PUBLICATIONS OF THE MINNESOTA ACADEMY OF SOCIAL SCIENCES

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PAPERS AND PROCEEDINGS

OF THE

FIRST ANNUAL MEETING

OF THE

Minnesota Academy of Social Sciences

EDITED BY

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PUBLISHED FOR THE ACADEMY

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The Minnesota Academy of Social Sciences

The people of a commonwealth can advance toward better conditions of government and more efficient administration only as public opinion grows more enlightened. Such public opinion is formed largely through the medium of the press, the schools, and associations organized to discuss questions of importance. With a view to providing a medium through which men may confer together upon important political, social, economic, and historical questions affecting the life of the state, the Minnesota Academy of Social Sciences has been organized.

It is believed that the influence of an organization whose members consist of persons interested in these questions would count much toward the formation of sound and rational doctrine relating to legislation and the social and industrial welfare of the people of Minnesota. It is equally certain that the publication of the papers presented at the annual meetings of the organization would stimulate thought upon these questions and that a journal would serve as a suitable means of communication between those interested in the public questions coming up from time to time in the State.

The absence of any state association dealing with these phases of social life suggests the creation of an association that would be state-wide and open to persons interested in these subjects. It needs no argument that the existence of such an organization with annual and special meetings held in the different towns and cities of the

State, and the publication of a journal devoted exclusively to matters interesting the citizens of Minnesota, would furnish a nucleus for an enlargement of public opinion on many questions.

To this end the Academy was organized in April of 1907, a constitution drafted and officers elected. The first annual meeting was held at the University of Minnesota, December 5 and 6, 1907.

The papers and discussions presented at that meeting are here embodied as the first volume of the proceedings of the Minnesota Academy of Social Sciences.

CONSTITUTION

I. NAME

The name of this organization shall be the Minnesota Academy of Social Sciences.

II. OBJECTS

(a) The encouragement of the study of economic, political, social and historical questions particularly affecting the State of Minnesota.

(b) The publication of papers and other material relating to the same.

(c) The holding of meetings for conference and discussion of such questions.

III. MEMBERSHIP

Any person approved by the Executive Committee may become a member of the Academy upon payment of two dollars and after the first year may continue a member by paying an annual fee of two dollars.

IV. OFFICERS

The officers shall consist of a president, three vice presidents, and a secretary-treasurer.

V. STANDING COMMITTEES

The committees of the Academy shall consist of an executive committee, a publication committee, and such others as may from time to time be required.

The executive committee shall consist of the officers of the organization and three elected members.

The publication committee shall consist of six persons appointed by the president.

The officers and members of committees shall hold their positions for one year.

VI. DUTIES OF OFFICERS AND COMMITTEES

The duties of the officers shall be such as usually pertain to such positions. The executive committee shall have charge of the general interests of the Academy. It shall have power to determine the time and place of meetings.

The publication committee shall have charge of the publications of the Academy.

VII. AMENDMENTS

Amendments, when approved by the executive committee, may be adopted by a majority vote of members present at any meeting of the Academy.

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The First Annual Meeting

The first annual meeting of the Minnesota Academy of Social Sciences was held in the auditorium of the Law School of the University of Minnesota Thursday and Friday, December 5 and 6. 1907. The attendance was large and the meetings successful. The program carried out was as follows:

PROGRAM

THURSDAY EVENING AT 8 O'CLOCK, DECEMBER FIFTH

HON. ROYAL A. STONE, Presiding

GENERAL PRINCIPLES

PRESIDENT'S ADDRESS—THE LEGAL BASIS OF TAXATION
Chas. B. Elliott, Associate Justice Minnesota Supreme Court.

ADDRESS—THE TAXATION OF CORPORATE PROPERTY AS SEEN IN THE TAXATION OF MICHIGAN RAILROADS
Robert H. Shields, President of the Michigan Tax Commission.

FRIDAY MORNING, AT 10 O'CLOCK, DECEMBER SIXTH

JUSTICE CHAS. B. ELLIOTT, Presiding

ASSESSMENT AND TAXATION OF REAL PROPERTY

REAL ESTATE VALUATIONS
Thos. A. Polleys, Tax Commissioner, C., St. P., M. & O. R. R.

THE WISCONSIN TAX COMMISSION'S VALUATION OF REAL ESTATE

Thos. S. Adams, Associate Professor of Economics, University of Wisconsin.

THE TAXATION OF RAILROAD PROPERTY

William W. Baldwin, Assistant to President C. B. & Q. R. R.

Chas. B. Miller. State Representative, Duluth.

FRIDAY AFTERNOON, AT 2:30 O'CLOCK, DECEMBER SIXTH

JUSTICE CHAS. B. ELLIOTT, Presiding

TAXATION OF PERSONAL PROPERTY

THE PERSONAL PROPERTY PROBLEM

Edw. A. Jaggard, Associate Justice Minnesota Supreme Court.

THE TAXATION OF CREDITS AND MONEY

Nils P. Haugen, Member of Wisconsin Tax Commission.

Carl L. Wallace, Secretary State Tax League.

THE MORTGAGE RECORDING TAX

Ambrose Tighe, State Representative, St. Paul.

THE BANKER'S VIEW OF THE MORTGAGE TAX

A. D. Stephens, State Senator, Crookston.

FRIDAY EVENING, DECEMBER SIXTH

Business Meeting—Election of officers, at Donaldson's Tea Rooms. 7 p. m.

Banquet—Donaldson's Tea Rooms at 8 p. m.

TOASTMASTER.

FRANK L. MCVEY, Chairman of Minnesota Tax Commission

"DEATH AND TAXES"
James Gray, Associate Editor Minneapolis Journal.

"I WOULD NOT TAX THE NEEDY COMMONS," Henry IV., Third Act.
O. M. Hall, Member Minnesota Tax Commission.

"HE TAXED THE LAND TO GIVE THEM MONEY." II Kings. 23, 35.
Mayor J. G. Armson, Stillwater.

"HE DAILY SUCH TAXATION DID EXACT." Daniel. Civil Wars, Vol. iv, 25.
Professor John H. Gray.

"ALL WENT TO BE TAXED, EACH ONE TO HIS OWN CITY." Luke 2, 3.
Ex-Governor John Lind.

REPORT OF SECRETARY-TREASURER

Early in 1907 a meeting was called to organize an Academy of Social Sciences. As a result of the meeting a committee on organization was appointed who reported back to the larger group on April 10, 1907. The constitution and by-laws presented by the committee were adopted and the organization completed by the election of officers. The topic of the first meeting was selected and the general subject "Taxation" adopted as the theme

of the two days' session. At a final meeting, October 28, 1907, the plans were completed, the tentative program prepared by the secretary accepted and provision made to carry out the plans. The sessions held in December which were the outcome of the plans of the Academy were well attended and the papers of unusual merit. The membership has grown preceptably and at the time of writing, March first, stood at 99.

During the period of the Academy's history, 10 months, the treasurer has received from all sources the sum of $218.00. The expenditures for the same period have been $108.73, leaving a balance on hand of $109.17, a sum that will have to be supplemented by the dues of 1908 and special pledges to meet the expenses of publishing the proceedings. The unusual advance sale of the proceedings, while gratifying, will not be sufficient to meet the cost. This is somewhat discouraging, though the rapid growth, and high position already won by the Academy among the organizations of the State is a matter of congratulation. The meeting of the coming year will be held in December. The general topic of that meeting will be the State of Minnesota. The program as now outlined by the committee is as follows:

(GENERAL SUBJECT)

THE COMMONWEALTH OF MINNESOTA

I.

GENERAL CONSIDERATIONS

1. The Commonwealth.
2. The Present Problems Involved in Minnesota's Statehood.

II.

MINNESOTA'S HERITAGE

1. Geographical and Geological Structure of Minnesota.
2. Forest and Iron Lands, Their Extent.
3. The Wealth of Minnesota.
4. Railroads in Minnesota.

III.

WHAT HAS MINNESOTA DONE WITH HER HERITAGE?

1. The Policy of the State Regarding Timber Lands.
2. The policy of the State Toward Ore Lands.
3. Policy of the State Regarding Agricultural Lands.
4. The Drainage System—Its Inauguration and extent.

IV.

1. The Population—Origin and Distribution
2. Social Legislation in Minnesota.
4. Minnesota's Educational System and Its Present Status.
3. Development of Charitable Institutions.

FRANK L. MCVEY,
Secretary-Treasurer.

Communications directed to the Secretary-Treasurer should be sent to the following address: 822 Seventh Street S. E., Minneapolis, Minn.

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Yardley, W. H.	St. Paul, Minn.
Young, F. G.	Eugene, Ore.

*Deceased.

First Session

GENERAL PRINCIPLES

THE LEGAL BASIS OF TAXATION

By Charles B. Elliott

It was thought appropriate that the session of the Academy devoted to the subject of taxation should be opened with a brief reference to the general principles which justify the imposition of taxes by the State and require their payment by individuals. It may be suggested that speculations as to the legal and moral basis and justification of taxation are unprofitable; that taxation no more requires justification than does the existence of the equator; that it is a condition of such universality as to justify itself by the mere fact of its existence. The consciousness of mankind associates taxes with the only other future event of absolute certainty. Although we all recognize that taxes and death are certain, the average man, especially if he be of substance, seems equally active in seeking to postpone the evil day when he must pay his debt to the State and to nature.

Burke characterized the discussion of the abstract right of taxation as belonging to the domain of political metaphysics—"the great Servonian bog, in which armies whole have sunk." But, nevertheless, in order to make

more endurable, if not more enjoyable, the performance of a public duty which the law imperatively imposes upon all over whose persons or property it spreads the protecting aegis of its power, it may be worth while to consider briefly the underlying principles which justify the State in appropriating a substantial part of the wealth of the community without the consent of the individuals who labor under the pleasing illusion that they are its absolute owners.

Probably the present idea of a tax is embodied in the statement of Bastable that: "It is a compulsory contribution of the wealth of a person or a body of persons for the service of a public power."[1] But history discloses the prevalence of various theories and diverse practices ranging from the voluntary gift of personal services to what the socialist writers call the "healthy habit of confiscation." J. B. Say says that the word tax is synonymous with calamity, and while as a definition this may not be strictly scientific, it contains elements which appeal to all of us. Then we have Colbert's statement, witty and yet philosophical, that the art of taxation "consists in so plucking the goose as to procure the largest quantity of feathers with the least possible amount of squawking."

Primitive government existed almost wholly for security and defense. The leader, whether priest, judge or warrier, who was responsible for this security, found some means of making the community supply the funds necessary therefor. In the beginning it is probable that the followers of this leader contributed their personal services out of fear or the feeling of personal loyalty to enable him to perform the public duties which he assumed or which were conferred upon him for the general good. In all such societies voluntary offerings consituated the first form of common contributions. Every man felt the necessity of upholding the political and

(1) Public Finance, p. 263.

military organization by his own personal offerings. As society advanced and the organization of the State became more complex and its activities more numerous voluntary payments ceased and individuals contributed from a sense of moral obligation. This obligation became ultimately a legal obligation. In early times the individual was forced to participate in the administration of government by personally aiding in public work, such as the construction of highways and bridges, the watch and ward of the community and military service. Such contributions were personal and were rendered irregularly, but for well defined objects and without any reference to the ownership of property. But as the institution of private property developed this personal quality of service gradually disappeared. The people were not yet willing to submit to a property tax. The king must, however, have revenue, and he raised it by covert methods. He concealed the tax under various more or less pleasing and effective disguises and resorted to subtle devices for the extension of his prerogative. Privileges and exemptions were granted for a compensation; fees and charges were imposed for what had theretofore been freely given. At this stage of development customs duties and impositions arose, and their manifold abuses made them forever thereafter unpopular. "The earliest manifestation of taxing power," says Seligman. "was generally merciless and brutal, and reacted on the public consciousness so as to stunt the growth of the feeling of obligation which had produced personal service." Or, as expressed by Baghot, "The primitive notion of taxation is that when a government sees much money it should take some of it, and that if it sees more money it should take more of it"

Notwithstanding the abuses of power which naturally led the people to look upon taxation as wrongful, there was finally developed in the mind of the individual the

sense of an obligation to contribute for the common good in proportion to his capacity. The growth of commerce made it necessary that there should be roads and canals and ultimately postal facilities. New government functions were gradually taken on. Education, the care of the infirm, the health of the community, required large public expenditures which necessitated increased taxation. Seligman has noted the stages through which this development passed. In the first the individual made a gift to the government; in the second the government humbly implored or prayed the people for support; in the third a dominant idea was that of assistance to the State, the contribution, while not exactly a gift, was nevertheless considered as a favor to the government; in the fourth the idea of sacrifice by the individual for the good of the state was prominent; in the fifth there was developed a feeling of obligation on the part of the taxpayer, and here we find the word duty used to describe the tax; in the sixth stage occurred the idea of compulsion on the part of the State and the contribution was termed an impost or imposition, which the Germans describe as *auflage,* something "laid on," and *aufschlag,* something "clapped on;" in the seventh and final stage we reach the idea of a rate of assessment fixed or established by the government without reference to the volition of the taxpayer.

The question asked by every taxpayer is, "By what right does that entity which we call the State, whatever may be its concrete form and whether its powers are exercised by a single man. by a single class or by a majority of citizens, take from the individual that which hitherto was absolutely his and null his ownership and convert the thing of value to its own use?" In other words, "Titus is to render to Cæsar that which is Cæsar's, but when Cæsar comes to take the shock of wheat or the firstling of the flock, Titus may well ask, as he

gives up, 'Why are they Caesar's rather than mine?'" Many attempts have been made to answer this question. It has been said that taxes must be paid because the State is the source of all title and the individual holds his property by grant or sufferance of the State, and in compelling contributions from its subjects the State is in the position of an owner who simply takes what is his own. Others have based the right of the State to take the property of the citizens upon the simple right of might and assumed that as a ruling power is physically able to take and apply what the individuals ruled over may call their own, it is legitimate and morally correct for it to exercise this right and take such part of its subjects property as it may see fit. The right has also been based upon the theory of an actual or implied contract between the State and the citizen, in virtue of which the State supplies a certain amount of protection of life and property, and for which the citizen in turn pays an equivalent in money, merchandise or personal service. This latter theory, which finds the justification for taxation in the fact of compensation given by the State, was very generally accepted by writers and statesmen a generation or so ago. Thus, Montesquieu wrote that, "The revenues of the State are the portion which each citizen gives of his property to have the remainder in safety and to enjoy it in comfort." The French National Assembly referred to taxation as "The common debt of all citizens and the price of the advantages that society affords them." Mirabeau said that, "Taxes are but advances made by taxpayers to obtain the protection of the courts and police." That is, taxation is only an advance to obtain protection for social order—a premium for insurance against social disorder. Proudhon asserts that: "Taxation is an exchange in which the State gives services and the contributor money." Modern authorities on economics discard this theory. Seligman says that,

"Until within a few years it was deemed necessary to base the theoretical justification of taxation on fanciful doctrines of contract, protection and the like." Bastable refers to it as the "once established and still generally popular doctrine that taxes are the price paid for the services of the public authorities." This way of looking at the facts, says he, "was quite in harmony with the political doctrines of the 17th and 18th centuries. Belief in a compact between the ruler and his subjects led naturally to regarding taxation as simply a payment for service done. A citizen received security and paid its price in taxation. The immediate advantage of the doctrine, as placing a limit to arbitrary exactions and tending to increase security, is apparent, and there is, accordingly, no reason for surprise when, in some form or other, the idea of exchange is associated with the payment of taxes." But the same learned writer asserts that: "The assertion that taxes are purely for services rendered is plainly untrue. We shall see that there is no possibility of measuring precisely the most important of the benefits rendered by the State. Security against aggression is, literally speaking, of "incalculable" good. Social order cannot be sold by retail like tea or sugar, and so is it with the other state functions, even the purely economic ones. Indeed it would be very near truth to say that the difficulty of applying the normal method of purchase makes a given form of activity suitable for state management; if defense and justice could be readily bought and paid for we might trust to private enterprise for a sufficient supply. Wherever benefit to the individual can be even approximately estimated there is a strong presumption in favor of levying the cost incurred from him and converting the tax into a fee. * * * The opposition between free payment and taxation is too important to be evaded by the introduction of a vague idea of an exchange of services as including

both, and any definition of taxation that implies or expressly states this combination is so far erroneous. Like the general doctrine of the social contract, its practical convenience as a weapon on the side of liberty cannot conceal its scientific weakness. The equivalence between the amount of taxes paid and the benefits obtained is rather to be found in the case of the community as a whole than of any special part of it. Looking at the public agencies from this point of view, it is well to conconsider whether the advantages of government are a compensation for its costs, and this test should be steadily applied in judging the merits of any proposed expeditures."

Methods of levying and collecting taxes are for legislative cognizance. The courts are not often called upon to find a theoretical basis for taxation. They deal with the subject in the light of conceded principles and limitations. The judges start with the fact that taxation is one of the necessary incidents of sovereignty, by virtue of which the sovereign power, the State, unless restricted by constitutional limitations, may appropriate the property of the individual even to exhaustion. In Weston v. Charlestown,[1] Chief Justice Marshall said that, "If the right to impose the tax exists, it is a right which in its nature acknowledges no limits. It may be carried to any extent within the jurisdiction of the State or corporation which imposes it, which the will of each State or corporation may prescribe." In the case of Loan Assn. v. Topeka,[2] Mr. Justice Miller said: "Given a purpose or object for which taxation may lawfully be used, and the extent of its exercise is, in its very nature, unlimited." This, of course, refers to the abstract of

(1) 2 Pet, (U. S.) 465.
(2) 20 Wall. (U. S.) 663.
See an article on the power of Congress to levy taxes solely for the purpose of destruction, in Mich. Law, Rev. Vol. 6, page 277.
(3) 195 U. S. 59.

power of taxation when no constitutional limitations exist. As expressed by Mr. Justice White[3] in McCray v. United States, where it was held that a tax imposed upon oleomargarine for the purpose of destruction was valid, "The taxing power conferred by the Constitution knows no limits except those expressly stated in that instrument." In North Mo. Ry. Co. v. Maguire[1] Mr. Justice Clifford said that, "Unrestricted by constitutional limitations, the only restraint upon the taxing power of the States is the responsibility of those in whom the power is lodged, and the power of appropriation of the proceeds when not so restrained is equally unlimited." Similar language has been used in many cases by the Supreme Court of the United States.

These limitations upon the sovereign power are imposed by the people in the form of constitutional provisions and possibly by the force of certain general principles and doctrines which lie at the base of the form of government. Judges deal with taxation as it is imposed and regulated by this system and their judicial duties are confined to seeing that the executive and legislative departments of the government levy and collect the revenues of the state with due regard to the interests of the State and the rights of individuals under the constitution and laws.

It is probable that in matters of doctrine and theory the law is never in advance of the average prevailing thought and sentiment of the community. The law is inherently and properly conservative and moves somewhere below the middle of the procession. In it is expressed the desires of the aggregate of average men whose consent must be won before the theories of the advanced thinker can be transmuted into legal realities. It is reasonable therefor to expect that when the courts attempt to state a theoretical or ethical basis for taxa-

(1) 20 Wall. (U. S.) 62.

tion they will be found a little behind the most advanced economists. They will probably express the doctrines of the leading authorities of an earlier generation. They are still more liable to feel no necessity for justifying taxation upon an ethical basis and agree with Mr. Justice Wayne[1] that the "necessity of money for the support of States in times of peace and war fixes the obligation upon their citizens to pay such taxes as may be imposed by lawful authorities." As said by Mr. Justice Peckham in a comparatively recent case,[2] "Taxation is eminently practical and is in fact brought to every man's door and for the purpose of deciding upon its validity a tax should be regarded in its actual practical results rather than with reference to those theoretical or abstract ideas whose correctness is the subject of dispute and contradiction among those who are experts in the science of political economy."

If further justification than the necessity of the State is required it is usual to find it in the theory that the taxpayer receives something from the State in return for the taxes paid,—some benefit which is substantially the equivalent of the property with which he parts.

Legal writers and the courts in judicial decisions have made very prominent this idea of compensation and the duty which the State is under to make an adequate return for the taxes paid. But this return need not be specific or in kind. The fact that it is vague, indefinite and uncertain will not invalidate a tax properly assessed and levied under legislative authority within the limits fixed by the constitution. According to this view the citizen is required to contribute to the support of the State, not because of any abstract duty or obligation, but because he receives from the State or the community something which is an adequate return for the money

(1) 16 Pet. (U. S.) 446.
(2) 173 U. S. 517.

which he pays. Numerous illustrations are found in the decisions. In People v. Mayer, Mr. Justice Ruggles said, "The right of taxation and the right of eminent domain rests substantially upon the same foundations. Compensation is made when private property is taken in either way. Money is property. Taxation takes it for public uses, and the taxpayer receives, or is supposed to receive, his just compensation in the protection which the government affords to his life. liberty and property and in the increase of the value of his possessions by the use to which the government applies the money raised by the tax. * * * * A rich man derives more benefit from taxation in the protection and improvement of his property than a poor man and ought therefore to pay more." In Mobile Co. v. Kimball[1] Mr. Justice Fields said that "taxation only exacts a contribution from individuals of the state or of a particular district for the support of the government, or to meet some public expenditure authorized by it for which they receive compensation in the protection which government affords or in the benefits of the special expenditure." Substantially the same idea is expressed by Mr. Justice Brewer in Ill. Cent. Ry. Co. v. Decatur[2] in the following language: "Taxes proper, or general taxes, proceed upon the theory that the existence of government is a necessity; that it cannot continue without means to pay its expenses; that for those means it has the right to compel all citizens and property within its limits to contribute, and that for such contribution it renders no return of special benefit to any property, but only secures to the citizen that general benefit which results from protection to his person and property and the promotion of those various schemes which have for their object the welfare of all."

Judge Cooley, in his well-known work on Taxation,

(1) 102 U. S. 703.
(2) 147 U. S. 197.

accepts this theory and expresses it in language which has been quoted in many decisions. "The justification of the demand," says the learned jurist," is found in the reciprocal duties of protection and support between the State and those who are subject to its authority and the exclusive sovereignty and jurisdiction of the State over all persons and property within the limits of governmental purposes. The person upon whom the demand is made or whose property is taken owes to the State a duty to do what shall be his just proportion in the support of the government, and the State is supposed to make adequate and full compensation in the protection which it gives to his life, liberty and property and in the increase in the value of his possessions by the use to which the money contributed is applied."

It is apparent that courts in dealing with the subject of taxation have generally accepted the theory that a man should pay taxes in proportion to the benefits which accrue to him from the State—"the so-called give-and-take or quid pro quo doctrine, also known as the enjoyment or bargain and sale—or exchange—or reciprocal—or social dividend—theory." It is easy to understand why this theory should appeal more strongly to the average man than the faculty theory. In the former the stress is placed upon the benefits to be received, while in the latter it rests upon the duty to be performed. The average taxpayer believes that there can be no justification for requiring him to contribute towards the support of the government unless he receives some adequate return for his money. The idea is elementary and readily grasped. Unless he is satisfied that the State will honestly perform its part of the bargain he will pay taxes unwillingly and under a sense of injustice, which, to his own mind, will excuse attempts to avoid payment.

But the economists now tell us that this theory of benefits has been discarded in favor of the theory that

men should pay taxes in accordance with their faculty or ability to pay. I do not find in a brief examination of the cases that many courts have had occasion to refer to the faculty theory, although the enactment of income and inheritance tax statutes has resulted in very full discussions of some of the general principles of taxation. The questions raised under these statutes have usually been whether the requirements of equality and uniformity have been violated by the provisions for graded or progressive taxes. Progressive taxation through inheritance tax statutes, which seem properly to rest on the faculty theory, has been generally, if not universally, sustained by the courts. Our own court in State v. Bazille,[1] has recently said that, "Ability or faculty to pay has come to be the test in determining the justness of taxation. It is 'not only the basis of taxation, but the goal towards which society is steadily working. It lies instinctively and unconsciously at the bottom of all of our endeavors at reform." Seligman, Taxation, 72. The equity and fairness of this theory, in its broadest sense, when we reflect upon the vast fortunes accumulated as the result of especially advantageous opportunities and facilities, not possessed by people in general, is apparent and obvious. It works no injustice or harm to those thus fortunately situated, does not injuriously affect industrial or productive agencies, and relieves in a measure those with better opportunities and those to whom taxation is always an extreme burden."

The notion that taxation is necessarily an evil belongs to a state of society which has generally passed away. It was a condition in which the citizens stood always in a relation of antagonism to the government; when the interests of the sovereign seemed always opposed to those of the people; when the theory that the State was the

(1) 97 Minn., 11.

source of title and that all property was held at the will of the State was a grim reality and not a mere theory; when Louis XIV could write in a memoir for the guidance of his son and heir, "To me belongs exclusively the lives and portions of my people. The nation resides entirely in the person of the monarch. Kings are absolute masters and may naturally, fully and freely dispose of all the property possessed by either the clergy or laity, to use at all times like wise stewards and according to the needs of the State." Under governments controlled by such doctrines taxes were in fact iniquities and constituted an awful burden upon the people. The subject was always a debtor of the State, and life was but a passage through a perpetual toll-gate. But these conditions no longer exist and taxation in a free popular government is not in itself an evil. On the contrary, it is the means by which civilization is developed and supported. The abuse of taxation is an evil, and it still, to some extent, prevails in all communities. This abuse consists not in the imposition of taxes, but in the unjust and unscientific methods which are still in vogue. As said by Wells, "There is no act which can be performed by a community which brings so large a return to the credit of civilization and general happiness as the judicious expenditure for public purposes of a fair percentage of the general wealth raised by an equitable system of taxation. The fruits of such expenditures are general education, general health, improved roads, diminished expenses of transportation and security for life and property. And it will be found to be a general rule that no high degree of civilization can be maintained in a community, and indeed that no highly civilized community can exist without comparatively high taxation. Meunier says that taxes properly raised "represent the investment of the capital of the nation or the State and general expense of its care and development." So, Cary

says that, "So far as is necessary for the security of persons and property money spent for the supporting of the government is as well expended as in the purchase of food and clothing."

Recognizing the truth of this statement, the citizen of a modern civilized democratic community can no longer feel that taxation is a form of robbery by which he is deprived of his property. He must recognize the fact that as a member of such a community it is his duty to bear a fair and equitable proportion of the burden of community life. He cannot close his eyes to the fact that schools must be supported, hospitals for the unfortunate maintained, roads and highways developed and property protected from fires and the ruthlessness of the lawless, and that all these things, without which modern society can not exist, require the expediture of vast sums of money. Ordinarily the State has no wealth in its own right except as it exists in the capacity and services of its citizens who control the property and wealth within its borders. Membership in the communities carries with it the obligation to share in the burdens incident to the life of the community. As we have seen, the recognition of this obligation is of slow growth and the readiness to share such burdens exists only in complex societies in which social ethics have been highly developed. It requires a developed sense of right and justice in the individual and a willingness to do what is right at some financial sacrifice.

It is obvious to even the most casual observer of present conditions that men who recognize this duty in theory systematically violate it in practice. It is not apparent that taxes are grossly excessive in view of the manifold demands upon the purse of the State and its subordinate agencies. Whether high taxes are an evil depends entirely upon the use to which the money is to be applied. I imagine that the principal difficulty at present is found

in the fact that the taxpayers are not satisfied that the taxes are equitably raised or wisely and economically expended. I doubt whether any intelligent citizen objects to the purposes for which taxes are raised and expended in this State. No one objects to paying taxes to support the schools, hospitals, police force, fire department, public parks, public libraries and construct and maintain creditable and artistic public buildings which tend to develop the State and educate the people. Nor is there any serious objection to taxation for the support and maintenance of the public service so long as it is felt that officials are not unnecessarily numerous and that their duties are faithfully and conscientiously performed; that they render an adequate return to the community for the compensation which they receive. Men who are not willing to pay according to their capacity for the support and maintenance of these things are unworthy of respect and are properly visited with the contempt of their fellow citizens. Of course, it is too much to expect that people will pay taxes cheerfully. Duties, public or private, are not usually performed in that spirit. But the average citizen expects to perform this duty, although it is unpleasant and involves sacrifice. Why, then, the common habit of tax dodging through false returns, unworthy shifting of funds and securities and the concealment of property? Simply because the feeling is prevalent that the system by which taxes are assessed and levied is inequitable and works injustice to certain individuals. I do not assume that even under an equitable system every citizen would willingly pay his taxes. The indisposition to part with his money without the prospect of an immediate return in some tangible form will always be stronger with many persons than the sense of obligation to the public. At the present time, under the system of a general property tax, no one claims that the result is equitable. Gross inequality of

burdens is imposed. Men do not pay in accordance with their capacities. The people do not share in the burdens of government justly and equally. It is not my purpose to consider this matter in detail, but think for a moment of the effect of a thorough appreciation of this one fact. A. dies impoverished, leaving a few thousand dollars of life insurance to his widow. It is all the property she has in the world. She loans it upon a mortgage which draws six per cent interest per annum and upon it he State levies a tax of three per cent.[1] That is, she pays a fifty per cent gross income tax, while certain public service corporations of the State pay four per cent gross income tax. There may be an explanation of what on the surface appears to be an unjust discrimination, but until that explanation is made in such form that it can be understood and appreciated by persons of average intelligence it is hardly reasonable to expect the widow to be satisfied with the results of taxation. Students of public affairs are earnestly endeavoring to devise a system of levying and collecting necessary taxes under which in equitable results will not be obtained. Let us hope that this Academy, through the intelligent study of these questions which incites and encourages, may be instrumental in bringing about a result so devoutly to be desired.

DISCUSSION

PROFESSOR RYAN: The compensation or benefit theory, which, according to Judge Elliott, is still the favorite theory of the jurists, seems to be out of harmony with many of the existing statutes. In our own State the inheritance tax is progressive, the rate increasing with the size of the bequest, while the smaller be-

(1) Since the above was written a mortgage registry tax law has been enacted (ch. 328, G. L. 1907). When this tax has been paid the mortgage is exempt from further taxation. The statute was held constitutional in Mut. Ben. L. Ins. Co. vs. Martin Co. (filed May 8, 1907.)

quests are entirely exempt. Small amounts of personal property are likewise untaxable. Moreover, the man without any property pays no taxes whatever except in localities where a poll-tax is still collected. On the theory that taxes are a compensation for benefits received by the taxpayer in the form of government protection to life, limb or property, such tax laws are inequitable, for the amount of the tax ought to be in proportion to the amount of protection, and the amount of protection varies exactly with the amount of property protected. At least this is the only practicable measure that can be applied to protection of property. With regard to life and limb, the protection afforded would seem to be greater in the case of the propertyless man than in the case of the man whose wealth enables him in some degree to protect himself. Consequently when the courts sustain laws of this nature they seem to sacrifice their theoretical views on the equities of taxation to the provisions of the organic and statutory laws of the State or of the nation.

It occurs to me that the compensation-theory owes a large part of its vogue to that political theory which regards government as the outcome of a social contract. In this view the citizen subjects himself to the authority of the State by the free surrender of a part of his independence. Therefore, the power of government over the individual must be interpreted narrowly, and the freedom of the individual widely. From this it follows that the State taxes the citizen in virtue of a power implicitly conceded by the citizen in the original compact, and that the citizen must be presumed to have limited this power in such a way that the taxes exacted should be equivalent to the legal protection rendered. Hence we find that Adam Smith and practically all the economists who were thorough-going believers in the political policy of laissez-faire and in the extreme doctrine of individual liberty were also adherents of the benefit-theory of taxation.

With the reaction from these theories of the relation between the State and the individual there has occurred, significantly enough, a departure from the compensation-theory. On the other hand, those who hold that the State is a morally necessary institution, reject the compensation-theory and maintain that the property-owning citizen is as truly obliged to pay taxes as the member of a family is obliged to promote the welfare of the family. According to this theory of the State, taxes are a burden imposed upon the citizen as a member of an ethically necessary society, and not merely a return for benefits received. Assessments for street improvements form no exception, since they are not taxes in the proper sense. Being a burden, taxes ought to be apportioned according to capacity. To use Mill's excellent dictum: "Equality of taxation means equality of sacrifice." Therefore the progressive tax is entirely equitable. For the larger a man's income, the fewer and feebler are the wants which will be deprived of satisfaction when a given per cent of his income is deducted. A larger rate of taxation on a larger income will, therefore, involve no greater burden or sacrifice than a smaller rate on a smaller income. Equal rates on widely varying incomes will mean inequality of sacrifice, and therefore social injustice.

C. J. BUELL: Whether a man should pay taxes according to ability, depends largely upon what is meant by ability. A man's ability to pay taxes is composed of two factors. First, his personal powers and capacities for productive labor; and, second, the benefits he derives from government.

Evidently no one should be taxed according to his personal strength and intelligence; at least, not until all have paid to the full extent of the benefits they have received. A sewer is built in front of my property, and I am called on to pay $112.74. This is fair, if only I am benefited to

that amount. Some years ago I had occasion to look up several hundred court decisions on this class of assessments, and in every case, the court held that any assessment for local improvements that was not in excess of benefits conferred was fair and just and must stand. And why should not such assessments stand? Surely no one should expect to get his sidewalks, sewers, and other local improvements at the expense of those who are not benefited. I have found that those who object to assessments for local improvements are usually vacant-lot speculators, who would like to get the benefits and have some one else pay the bills. It would be just as fair to ask some one else to pay for their food and clothing.

And the same principle will apply to all really needed public work. Every move in the direction of good government, every step in social development creates benefits equal to, or in excess of, the cost of such improvements. And all these benefits manifest themselves in higher prices for land. Just as the sewer, the water main, and the sidewalk add to the value of adjoining lots more than their cost, so do schools, police protection, clean streets, make a town more desirable to live in, and cause the price of lots and lands to advance. And the value of lots and lands is the only value that is enhanced by good government. Houses are worth what it will cost to replace them, unless in a dying town. Clothing and food, and all the comforts and luxuries of life are governed in price by the value of the labor it will take to replace them; and none of these things are increased in value by any sort of public improvements, or by any kind of good government. On the contrary, all the products of labor are cheaper in well-ordered communities; because of the greater ease of supplying the demands of the market.

But the value of the land—that increases with every

new school house, every paved street, every improvement in police protection or sanitation, every advance in public morals, every addition to population.

Here is the natural law. Government is a natural thing, founded on a law of nature as unyielding and as beneficent as the law of gravitation. There must be a natural source of public revenue—a natural system of taxation. And this natural system is not the system that sneaks around and spies out the number of pots and pans, of beds and chairs a man possesses, and then taxes him for having them; not the system that fines a man for building a home to shelter his wife and children; not the system that harasses and hampers his business and his industry; not the system that robs the widow and the orphan of the meager inheritance left by a loving father called to his rest; not the system that plunders a man of a part of his honestly-earned income.

No, none of these; but a natural, just and honest system that takes for common use the values that the public as a whole has produced—the values that attach to land because of social growth and progress. These values, publicly produced, naturally belong in the public treasury, and they are the only values that the public has any moral right to take for public purposes. And just as assessments for betterments are right and fair up to the full amount of the benefit conferred, as the courts unanimously hold, so these land values, created by the public, belong to the public, and ought to be taken and used for public needs.

When this is done, land speculation will cease. The gigantic fortunes of landlords and franchise grabbers will end. There will be no abnormal income, no swollen fortune to be inherited. But the resources of the earth will be easy to get by him who wants to work; and all may live in comfort and peace on the products of their labor and

skill, undiminished by government tax or toll, untouched by monopoly's robbing hand.

This is the natural law,
  This is the law divine
That plainly marks what things are ours
  And what are *mine* and *thine.*

"THE TAXATION OF CORPORATE PROPERTY AS SEEN IN THE TAXATION OF MICHIGAN RAILROADS"

By Robert H. Shields

During a recent visit in the city of Detroit my attention was directed to an inscription, chiseled into the base of a statue, erected to the memory of the late Governor Hazen S. Pingree of Michigan. This informs us that "He was the first to warn the people of the great danger threatened by powerful private corporations and the first to awake to the great inequalities in taxation and to initiate steps for reform."

Mr. Pingree was governor of Michigan during the years 1897 to 1900 inclusive, so that the agitation for a more equitable system of taxation among corporations began ten years ago, and has been a leading issue in Michigan politics during all that time; and, although, at the present time, there exists many inequalities in Michigan's system of raising and distributing its revenue, no well informed citizen of the State will deny that many reforms along the line of corporate taxation have been inaugurated.

Previous to the time indicated there was no apparent uniformity in taxation. Notwithstanding the fact that the law required all property, not exempt from taxation, to be placed upon the assessment roll at its true cash value, there were almost as many standards of value as there were assessing officers. The assessing officer who succeeded in keeping his total assessment furthest away from the true cash value of the property in his district seemed to be the most popular with his constituents and

was generally the hardest man to beat at the polls. It was apparent to all who had given the subject the slightest attention that there was absolutely no equality in the tax burdens, either among the general properties, assessed by the ad valorem plan, or between the general properties and those corporate properties paying taxes by the specific method. On the contrary, the very rankest kind of inequality existed among all property. To be sure, the boards of equalization were supposed to equalize matters, but here, too, the man of influence too often prevailed against the commands of the law and the situation, as a matter of course, became intolerable. Then, too, it was notorious that properties paying taxes under the specific plan were not paying anything like their just proportion of the State's burden. The pendulum of unequal taxation had swung the limit.

Under this chaotic condition of the tax affairs of our State, it did not require much agitation during the campaign of 1898 to arouse the people to the point of demanding that a more equitable and just system of taxation be established, and so, as a result of the election that followed, the legislature of 1899 took up the taxation problem along those lines.

This legislature passed an act creating a board of State tax commisioners. The act was an amendment to the general tax laws of the State and provided for the appointment by the governor of three resident freeholders to constitute the board. The act imposed many important duties upon this board, among which were: that it should have general supervision over all the assessing officers of the State and take such measures as to secure the assessment of all the general properties at actual cash value; to confer with and advise assessing officers as to their duties, and to prefer charges against those who were derelict in duty in reference to assessment and taxation; to investigate conditions of property

and to receive complaints respecting the same and take proceedings to correct any illegality found to exist; and also to investigate and ascertain the true value of the properties then paying taxes by the specific method, as well as the true value of all other properties paying by the ad valorem plan, and to report to the legislature the conditions and values found to exist, to the end that it would have the information necessary to rearrange the rate or system of taxation so that all taxable property of every description would pay taxes uniformly and on an equal basis.

The new commission organized at once and went to work with a will and a dash that really deserved a better fate. A tax commission in Michigan, with executive powers, produced more than a startling effect upon the assessing officers of the State and. naturally, its results were watched with more than passing interest by the taxpayers. The duties of the commission were not only many, but carried with them a great amount of labor as well as great responsibility. And there were no rules or precedents, no organization or blanks or guide to assist or point the way.

Their attention at first was naturally directed to the larger corporations and the result of their first year's work showed an increase in the assessment of real estate from $825,858,000 to $1.006,453,000, and in personal property from $142,330,000 to $310,997,000, or a total increase of $349,000,000, this increase coming largely from mining and other corporate property comprising over 1,200 corporations. Much bitterness was engendered throughout the State because of some of the methods employed by the commission in prosecuting its work and when the new legislature assembled in 1901 the commission was subjected to a reorganization and the membership increased from three to five, only one member of the former board finding a place on the new commission.

The new commission, having the benefit of the experience and results of the work of the former commission, proceeded in its work along more methodical lines. They undertook to revalue the property of the whole State by assessing districts to the end that all the property would find its place upon the assessment rolls and at its true cash value. For this purpose a large force of experienced men, in most cases former supervisors or assessing officers, were employed. These men were called "field men." To begin with, a memorandum of all sales of real estate in the assessing districts of a county, by warranty deed, and covering a certain period, obtained from the registers of deeds, was placed in the hands of these field men. They then ascertained the actual consideration passing between the parties to a sale, by inquiry of one or both of the parties, or of the supervisor of the township in which the land conveyed was situated, or of other well-informed persons of the township. The property sold was also carefully examined and its value estimated and inquiry made to learn if the sale was made at what might be considered the normal or usual selling price of the property, or if the sale was made under unusual circumstances which made the consideration of sale higher or lower than the normal or usual selling price. As many things influence the sale of property and the considerations of sales, it was the duty of the field men to learn the true conditions so that only sales of property at the usual selling prices should be taken as a criterion of value.

And in addition many other parcels of property were examined, at least one parcel in each section of land in a township and all kinds of property and in all portions of a village or city, and the value of each parcel carefully estimated and noted. In cases of properties sold verified considerations were compared with the assessments of the same properties and percentages obtained; and the

estimated values of unsold properties were also compared with the assessments of those properties and another percentage obtained. Either percentage, or the average of them, as was sometimes taken, was valuable and showed very clearly the character of work of the assessing officers in the townships and districts examined.

Notwithstanding the great care and skill with which this class of work was done, occasional errors were made which were quickly and eagerly taken advantage of by certain assessing officers who were unalterably opposed to any outside interference with their assessment rolls. Nevertheless, except in a few counties, where unusual conditions prevailed, notably the mining counties, the results were approximately correct. And that the use of this data by the supervisors as a guide to future assessments, and by the tax commission as a basis of changing assessments, or by a board of supervisors in its work of equalization, would produce better results all round our commission is fully satisfied.

And from the fact that in the prosecution of this work by the tax commission practically the same amount and character of examination was made of the property of each and every assessing district of a county, that the same quality or character of judgment was exercised as to all portions of the county; that these examinations were made and judgment expressed by intelligent, experienced men, free from local bias and unmoved by local influence, it is clearly evident that the results should be a better knowledge of value of the property in the entire county, a better knowledge of the relative value of the several assessment districts of a county and a better knowledge of the comparative character of supervisors' assessments than any plan formerly employed by the various assessing officers of the State. This plan of work continued for over three years and some seventy counties of the eighty-three in the State covered.

The total assessment of the general properties in the State had increased from 1899 to 1905 over $600,000,000. But these results were not received with unbounded enthusiasm nor was the work of the commission altogether popular among the people. To be sure the commission was commended as long as it confined its work to the next county. It was equally popular while employed in boosting the valuations of mining and other corporations. But when this had been accomplished and it began to make universal application of its efforts to obtain equal taxation its popularity rapidly began to wane. It apparently had outlived its usefulness and in the fall of 1905 the commission was again reorganized and reduced to three members, only one of the old board becoming a member of the new commission. At the same time it was practically stripped of its former powers as regards the general property of the State and under the present law can only interfere with local assessments after a written complaint has been made by a resident taxpayer of the district in which the assessment complained of is made.

Such is a brief history of the board of State tax commissioners of Michigan, a recital of which I thought might be of passing interest at this time.

While our commission still has an important function to perform in adjusting differences arising between the assessing officer and the aggrieved taxpayer, its usefulness as a commission whose original purpose was to inaugurate a system of equal taxation throughout the State no longer exists. All of which leads one to the conclusion that the day of equal taxation will not be here until the Golden Rule has a more universal recognition.

I have spoken thus far of the board of State tax commissioners. But the members of this board were, in 1901, made, *ex-officio,* members of a state board of assessors, whose duty it is annually to make an assessment at true

cash value of all property having a situs in the State, such as railroad companies, express companies, sleeping car companies doing business within the State, car loaning companies and refrigerator and fast freight line companies, as well as all other corporations owning, leasing, running or operating over or upon the lines of any railroad in the State, any freight, stock, refrigerator, or any other cars, not being exclusively the property of a railroad company paying taxes upon its rolling stock under the provisions of the act creating the board.

Here was the first attempt in Michigan to apply the ad valorem plan in the assessment of railroad property and that of the other companies mentioned, as formerly the railroads, as well as the other companies mentioned, that paid any taxes at all, paid a specific tax based on gross receipts. The enactment of this law followed the investigations made by the board of State tax commissioners in 1899 and 1900. It will be remembered that it was made the duty of this board to investigate and ascertain the true cash value of the properties of corporations paying specific taxes and the rate of taxation paid on such valuations, so that comparison could be made between the properties paying taxes under the specific method with those paying under the ad valorem plan.

Of course, the railroads were the principal object against which the batteries of the new state board of assessors were directed. But how to arrive at the "true cash value" of the railroads seemed for a time to baffle the members of the board. Theories of all kinds were advanced, all possessing some merit, but in the practical application of any one of them some weak point would be disclosed that would render its general application impracticable. Correspondence was had by the original tax commission with nearly every other State in the Union and replies received from most of them. Their

specific methods were inquired into, the manner in which valuations were made and the thoroughness with which it was done. It may be said that, after a careful study and examination of the plans and methods pursued in all these States, and considering the results accomplished, not one of them seemed to offer a fair or satisfactory solution of the problem and the result was to add still greater confusion to an already confused situation.

One of the theories advanced suggested the payment of a tax based upon the par value of the stock; but a variation of the stock from three to three hundred per cent, as investigation showed to be the case, proved that this theory is not susceptible of any meritorious defense.

Another theory proposed to find the actual value of the railroads from the value of the stock as shown upon the market, or, in other words, to estimate the value of the road by the market value of the stock alone. But this method would not take into consideration the bonded indebtedness of the road; and as few, if any, railroads are without an indebtedness of this kind, a general application of this method would be incorrect and unfair. To illustrate, a railroad may have stock worth on the market, say twenty-five cents on the dollar, making the total stock worth say, $2,500,000. At the same time the road may be bonded for $5,000,000 and the bonds perfectly good. Since the stock is subject to the bonded indebtedness it is very plain that the market value of the stock could not reflect the actual value of the railroad property.

To value the railroads upon the market quotations of both stocks and bonds is another theory that claimed many supporters. But as far as applying this theory to all roads in Michigan was concerned it was found to be impracticable from the fact that the stocks and bonds of not more than a dozen railroads were quoted in the market, that the stocks and bonds of the other railroads

were unknown to the open market and that such a method could be applied only to the few quoted. Then, too, the computation of the bond values is rendered intricate and uncertain by reason of the fact that there may be several different issues of bonds issued by a company upon different portions of its line or upon the same portion of its line, or an issue may cover a line partly in the State and partly in an adjoining State; or an issue may have been made at a certain time covering the whole line, since which time the line may have been extended without it appearing how the issue is affected, or in what manner.

Another great difficulty encountered in applying the stocks and bonds method in arriving at the valuations of railroads lies in the separation of railroad property devoted to operation from the property owned by the railroad, but not used in its operation. The stocks and bonds of a railroad company represent the value of all the property of the company,—whether devoted to operation or not,—manufacturing plants, real estate, mines, elevators, warehouses, stocks and bonds in other corporations, etc. This latter property is subject to local appraisal and taxation. To ascertain and separate all these items and make the proper deductions from the total value represented by the stocks and bonds would involve more time and labor than the ends would seem to justify. And when we further consider the intricacy and uncertainty of the computation of stocks and bonds values, the manipulation by stock brokers, regardless of actual value, together with the very many conditions that affect the price or value of the stocks and bonds regardless of the real property itself, we can readily appreciate the incompetency and unreliability of this method to place a correct value on the railroads of Michigan, or, indeed, on those of any other State.

Still another theory named the cost of construction, as shown by the general balance sheet of the company, as

the best available measure of the value of railroads. This method, however, had few supporters outside of a few railroads that would be distinctly benefited in its application, and it received very little consideration at the hands of the commission.

Another theory would determine the value of the railroads by capitalization of the net income. There is much to be said in favor of this method and there would be more if the actual net earnings could be determined by a state board, which, under the present system of accounting by the railroads, seems well nigh impossible. But one serious objection to this method is that it assumes a net surplus at all times and never a deficit. The practical difficulty then would be that, strictly applied, it would result in wiping property which has no net income off the rolls entirely, which is hardly in harmony with the general principles underlying the scheme of taxation in Michigan.

But the method that claims the greatest number of adherents in Michigan is what is called "The inventory method supplemented by a consideration of the effective earning capacity of the roads." Probably in Michigan this is better known as the Cooley-Adams method. This method contemplates a complete inventory of all the physical elements of the road, showing the cost of reproduction and the present value supplemented by a capitalization of the net corporate surplus earnings. This scheme of railroad appraisal received its first application in 1900 in Michigan, its execution being placed by the tax commission under the supervision of Prof. Mortimer E. Cooley, dean of the Department of Engineering of the University of Michigan, and. admittedly, a gentleman of great engineering skill and ability. In his appraisal of the so-called physical or tangible elements of the Michigan railroads Mr. Cooley proceeded in the same manner as if a new road were projected in the exact location of

the present road, and computed the cost of building and equipping the road to the extent already existing, everything being new, and then, allowing for depreciation where deemed necessary and proper, fixed other values representing the actual or present condition of those elements subject to change with time. This work included a careful inventory and inspection by competent engineers of practically every locomotive and passenger car belonging to Michigan railroads, as well as all shop machinery and tools, locomotive, passenger, freight and miscellaneous equipment and of all stores and supplies. Experienced railroad engineers proceeded over the different railroads by means of hand cars or on foot and made a personal inspection of all the railroads in the State. The work was classified under thirty-seven different items, or accounts, and included: Engineering! right of way and station grounds; real estate; grading; terminals; bridges; culverts and trestles; ties; rails; track fastenings; frogs, switches and crossings; ballast; track laying and surfacing; fencing; cattle guards and signs; interlocking and signal apparatus; telegraph; stations, buildings and fixtures; shops, round houses and turn-tables; shop machinery and tools; water stations; grain elevators; warehouses; docks and wharves; miscellaneous structures; locomotives; passenger equipment; freight equipment; miscellaneous equipment; telephone; ferries and steamships; electric plants; terminals; legal expenses, interest; miscellaneous expenses; stores and supplies.

The result of this most complete inventory showed the total cost of reproduction of the railroads of Michigan to be $202,716,262, and the "Present Value," that is, the value after allowing for depreciation, $166.398 156. But this was an appraisal of the physical elements of the railroads and did not presume to represent their actual or cash value. It was said that in many of the railroads there existed non-physical, or intangible, or franchise ele-

ments, possessing a value beyond that found in the appraisal of the physical properties. Mr. Cooley's part of the work being completed, the rest of the work embraced in this general plan was placed in the hands of Prof. Henry C. Adams, professor of political economy at the University of Michigan, and statistician to the interstate commerce commission. And no one more familiar with the work at hand, nor better fitted by education and experience to cope with this subject could have been chosen.

The rule submitted by Prof. Adams for the determination of the non-physical values of railroad properties is as follows:

1. Begin with gross earnings from operation, deduct therefrom the aggregate of operating expenses, and the remainder may be termed income from operation. To this should be added income from corporate investments, giving a sum which may be termed total income, and which represents the amount at the disposal of the corporation for the support of its capital and for the determination of its annual surplus.

2. Deduct from the above amount, that is to say, total income, an annuity properly chargeable to capital, a certain per cent of the appraised value of the physical properties.

3. From this amount should be deducted taxes, rents paid for the lease of property operated, provided such property is not covered by the physical valuation made the basis of the annuity referred to under paragraph 2, and permanent improvements charged directly to income. The remainder would represent the surplus which, capitalized at a certain rate of interest, gives the value of immaterial properties.

The following illustration will show the result of the application of the Cooley-Adams theory, or plan, or the "Inventory method, supplemented by capitalization of corporate surplus earnings:"

Prof. Adams found from the average gross earnings of the Michigan Central system for the years 1898 to 1902, inclusive, that the average net earnings amount to.....$3,620,377
The Michigan proportion, based on track mileage, was 2,503,345
Mr. Cooley had appraised the physical elements at 45,438,599
Prof. Adams allowed an annuity of 3½ per cent on the physical elements, or..... 1,590,351
He then deducted this amount from the total net earnings, leaving a remainder of..... 912.994
This amount was then capitalized at 5 per cent to determine the value of the non-physical elements. which amounted to.....18,259,880
To this amount was added the value of the physical elements appraised by Mr. Cooley at 45,438,599
And the total value of the road in question was fixed at.....$63,698,479

It is very patent that in the application of this unique method of appraising railroad property everything depends upon the percentage adopted. For instance, if an annuity of 4½ per cent had been allowed instead of 3½ per cent on the physical properties and the surplus corporate earnings capitalized at 6 per cent instead of 5 per cent, which would appear just as equitable, the value of the road would be $53,070,000. Or, if the inventory part of this theory be disregarded entirely and the net earnings be capitalized at 6 per cent the result would show a valuation of the Michigan Central system in Michigan of $41,722,416. Or capitalizing the net earnings at 5 per cent the value would be $50.066,700.

Plausible as it may appear, however, this ingenious method does not entirely fill all the requirements of the case at hand. at least not as it was applied in Michigan. In the first place, it will be observed that at any stage

of the process a deficit might be discovered, and where such was actually the case, the physical value as found by Mr. Cooley was taken and regarded as the value of the property. The rule, apparently, does not work both ways. Now, as a general principle: If the amount as shown by the physical appraisal of a railroad property which earns *more* than a fair percentage of profit does *not* represent its actual cash value, neither does the physical appraisal of a railroad property which does *not* earn a fair percentage of profit represent *its actual* cash value. And in this connection it may be of interest to state that in the Cooley-Adams appraisal of Michigan railroads a non-physical value was placed on only twenty-six of the 123 railroads appraised, and the physical appraisal made by Mr. Cooley was adopted as the actual cash value of the other ninety-seven roads.

The physical value of the twenty-six railroads in which was discovered a non-physical value amounted to $101,093,512, and the non-physical value of the same $35,814.043. The physical value of the remaining ninety-seven railroads amounted to $65,304,644, which amount under the plan in question represented the value of these railroads.

An analysis of this theory, therefore, discloses the fact that in reality two distinct methods are employed in valuing the same class of property. The method employed in valuing those ninety-seven railroads that did not earn a profit, or, at least, that did not earn more than a *fair* profit, is the inventory plan pure and simple whereby the value was determined by an inventory of the physical elements only. While in the valuation of those twenty-six railroads earning more than a fair profit the capitalization of a portion of the net earnings followed by a further capitalization of the surplus net earnings is the method employed. This latter method, regardless of its mysterious appellation, is a tax based upon the net income.

Here, then, we have two different methods or standards of valuation employed in valuing the same class of property which is hardly in harmony with the constitution and laws of our State.

But there is another reason which would preclude the application of this theory in its entirety in assessing Michigan railroads.

The rate of taxation applied to the assessed valuation of the railroads in Michigan is the average rate of taxation levied upon other property of the State upon which ad valorem taxes are assessed for State, county, township, school and municipal purposes. Now this theory is applicable to a considerable amount of other property in the State, but is applied in not a single instance by any of the seventeen hundred assessing officers. And, furthermore, because of the technical skill and theoretical training required for its intelligent application, it is not likely to be adopted. It would, therefore, be manifestly unfair and unjust to adopt this plan in the assessment of the railroad property in the State unless the same plan be adopted in the assessment of all other property to which this theory might equally apply. If we were to apply this theory in the assessment of all the property to which it might be applied with equal consistency the assessment rolls of the State would show a total nearer $5,000,000,000 than $1,598,935,606, which is the aggregate of the assessed property for the year 1906.

The pendulum of unequal taxation in Michigan, as far as the railroads are now concerned, has already pretty nearly swung the return limit, and a strict adherence to this theory in assessing Michigan railroads, considering the methods employed in assessing other property would not only not be a square deal, but would mean nothing more nor less than confiscation. The results obtained by this plan, however, are generally used for

comparison to discredit the work of the State board of assessors.

In determining the amount of tax which shall be imposed upon corporate property, the question of method must always be subordinate to the other question of the equity of the result which follows it; and, other things being equal, preference should always be given to the most simple and effective method.

It is impossible to arrive at the true cash value of a railroad property, or of any corporate property, unless all the elements which enter into and make the cash value be considered.

No hard and fast rule, or theory, can be employed in the valuation of corporate property.

In determining the true cash value of railroad property it is proper to take into consideration the cost of reproduction, its value after allowing for depreciation, its location, its gross and its net earnings, or the fact that it is not earning a fair profit, the permanency and general character of its business, the par and market value of its stocks and bonds, its connections and terminals, and in short every element and condition that adds to or detracts from its supposed value. But each railroad stands alone. And no theory yet advanced can be arbitrarily employed in fixing the values of each and every road without working the rankest kind of injustice on some of them.

Michigan railroads are now assessed under the ad valorem plan. Previous to the organization of a State board of assessors they paid taxes under the specific system. A comparison of the amount of taxes paid by Michigan railroads for the last four years under the specific system with the amount paid for the first four years under the ad valorem plan, reveals the interesting fact that the taxes of the railroads have increased 131 per cent, not including penalties exacted amounting to $1,158,200, while taxes levied on the general properties of the

State have increased less than one per cent. The same comparison shows that while under the specific system the railroads paid an amount equal to 42 per cent of the State tax, under the ad valorem plan they pay 103 per cent.

But it may be remarked that if, perchance, the Michigan railroads are now paying more than their fair share of the State burdens, they may derive some consolation by regarding the excess as a penalty for the violation of the Golden Rule of taxation in the past.

The relation which railroad taxes have born to State taxes for the four years preceding the change from the specific to the ad valorem basis and for the four years succeeding such change is shown in the following table.

	Railroad Taxes	State Tax
1898	$1,091,526.39	$2,158,770.67
1899	1,240,745.27	3,725,872.87
1900	1,356,857.96	2,908,801.59
1901	1,483,906.95	3,835,888.19
Total	$5,173,036.57	$12,629,333.32
1902	$3,288,162.06	$2,669,875.29
1903	3,756,149.42	4,003,255.11
1904	3,330,350.59	2,958,004.98
1905	3,527,059.61	3,871,080.34
Total	$13,901,721.68	$13,502,215.72

For many years railroad influence controlled the politics of the State and railroad property did not pay its fair proportion of the taxes. But this condition no longer prevails. Indeed, at the present time politicians regard the open support of the railroads as fatal to their ambitions and many of them get red in the face and hoarse in the throat in frantic efforts to ally themselves upon the side of the dear "pee-pul" whenever the word "railroad" is mentioned in their presence. Today in Michigan railroad corporations have no rights that politicians are bound to respect.

As to "equal taxation," which was Mr. Pingree's slo-

gan, we are getting as far away from it as when he first sounded the alarm.

The tax commission on the one hand has been virtually stripped of its power to regulate the assessment of general property. On the other hand, theoretical experts have been employed, at great expense to the State, who, in the application of certain theories regardless of the equities, have placed the highest possible valuations upon the railroads and the State board of assessors are asked to levy against these valuations the "average rate" of taxation levied upon all the other property, notwithstanding the fact, well known to all outside of the asylums, that the real estate of the State is not assessed at more than two-thirds its cash value and that not 25 per cent of the value of the personal property finds a place on the assessment rolls, resulting in an "average rate" far in excess of what it ought to be.

An official whose desire is to be fair ought to hesitate before adopting these theoretical valuations as the "true cash value" of the railroads and applying to them the "average rate" so obtained.

Our board refused to adopt these theoretical valuations, and while our action is approved today by the thinking portion of both people and press, it afforded a splendid issue for the high soprano politicians who saw an opportunity to further their own ambitions in a finely executed grand stand appeal to the credulous part of the public.

The people may be fooled occasionally, as they undoubtedly are. Their disposition, however, is to be fair and the existing wrongs in taxation matters will be righted when properly shown.

Even now it may be truthfully said that, with a few notable exceptions, the tax laws of Michigan are fair and equitable. The fault is not so much with the law as with the manner of its execution.

The railroad corporations, as a whole, are now paying at least their share of the taxes and the smaller industrial corporations are paying on the same basis as other property in their respective districts. There still remains a few large public service corporations who have so far succeeded in evading the payment of their fair proportion of the State burdens; but their day is surely coming, and if they are wise they will benefit from the experience of the railroad corporations and get under cover before it is too late.

Second Session

ASSESSMENT AND TAXATION OF REAL ESTATE

REAL ESTATE VALUATIONS

By Thos. A. Polleys

Real estate constitutes the major part of our national wealth. As measured by the assessors in Minnesota and most other States of the middle west the value of real estate comprises from 70 to 80 per cent of the grand assessment roll. Such will probably continue to be the case for many years to come.

The determination of the proper value to be attributed to real estate is of more far-reaching importance than any other single question among all the various questions which are presented from year to year to the consideration of either the State or the local tax authorities. But in most instances the methods employed by such authorities for the solution of this great problem are unnecessarily crude and unscientific, and the results worked out thereby fall correspondingly short of that degree of exactness and equity which might reasonably be attained and thereafter maintained. It is the chief purpose of this paper to present for consideration certain methods which, it is believed, would if put to general use by the tax authorities, in conjunction with such other methods as are also useful, soon result in a more accurate and equitable determination of realty values.

The laws of most States require that real estate shall be assessed for taxation at its full true value, though in some States, as in Iowa and Nebraska, it is provided that the assessed value shall be only a certain portion of the actual value, as one-fourth or one-fifth. Real estate, as a whole, is probably not assessed at its full value in any of the States which require that it shall be thus assessed and in very few is it assessed at more than one-half of true value. In almost every State it is the duty of some state board to attempt to properly equalize from year to year the assessed real estate valuations between the several counties of the State; and within each county it is the duty of the county board or county commissioners to annually attempt a like equalization of realty valuations as between the several townships, cities and villages within the county.

It is hopeless to expect that aggregate real estate valuations as between the several counties or as between the minor subdivisions within the county can be equalized at a substantially uniform percentage of true value unless and until some reasonably accurate process is employed for the determination of the full true value.

Some years ago, soon after its organization, the Wisconsin tax commission originated the process which it has ever since used for the determination of the true aggregate value of real estate in a given assessment district or county. Under the influence of the tax commission, exercised largely through the county supervisors of assessments, this process is being more and more used by the various county boards as an aid in equalizing real estate valuations as between the towns, cities and villages. It has been used by the tax commission itself for six years past as its guide in the equalization of realty valuations between the respective counties.

The methods of the Wisconsin tax commission in the valuation of real estate are to be discussed in de-

tail at this session by Dr. Adams and it is unnecessary for me to comment upon them at this time, except in a general way. For my present purpose it will be sufficient to quote the following brief description of the process as stated by the Commission on pages 17 and 18 of its report issued in 1907:

"The plan pursued has been to ascertain the consideration paid for lands sold in each assessment district during each of five years, and the last assessment of the same lands returned for each of the same years, and to find the true value of the district by applying the ratio of assessed to true value of the lands sold to the aggregate assessed value of the real estate of the district; then adding together the yearly aggregates and dividing the sum by five to get the average for a single year.

"In a general way the formula for ascertaining the true value of real estate may be stated thus: As the assessed value of the lands sold is to the consideration paid for them so is the assessed valuation of the real estate of the entire assessment district to the full value thereof."

Thus it is seen that the Wisconsin plan is one for the ascertainment of the aggregate true value of all taxable real estate in a given assessment district treated as a unit. The evidence tending to prove the essential accuracy of results worked out by this process will no doubt be fully presented by Dr. Adams. I deem it proper, however, to call attention at this time to the striking manner in which the accuracy of such results is corroborated by results worked out by use of probate appraisals.

In Wisconsin probate appraisals of real estate were gathered for the years 1904 and 1905 in twenty-eight counties, most of which were located in the southern part of the State. Opposite the appraised value of each parcel was set down the amount at which that particular parcel was assessed for taxation in the year of the ap-

praisal. The appraised values and the assessed values of all the parcels appraised in each year in each of the counties were then added together. The total assessed value of the parcels appraised was next divided by their total appraised value, the quotient being the average ratio of assessed value to the value fixed by probate appraisals. The total assessed value of real estate in each county for each year was then divided by this average ratio of assessed value to appraised value, the quotient being the approximate sum at which all the taxable real estate in the county would probably have been appraised in probate court in such year. Adding together the results for the twenty-eight counties for the year 1904 the conclusion was reached that the total value of all taxable real estate in those counties in that year would have been fixed by probate appraisers at a little less than $844,000,000. The Wisconsin tax commission, by the application of their formula above quoted to the land sales for the single year ending August 31, 1904. worked out the total realty value in 1904 of the twenty-eight counties in question at the aggregate sum of a little over $951,000,000 as against the $844,000,000, at which it would have been appraised by appraisers in probate court. A similar series of computations showed that the total realty value of the twenty-eight counties in 1905 would have been fixed by appraisers in probate court at approximately $877.000,000 as against a total realty value for them in that year, as determined by the tax commission by the use of land sales for a single year only, of a little over $991,000,000. It is interesting to note that the increase in the 1905 total realty value of the twenty-eight counties, as estimated from probate appraisals, over its value on the same basis in 1904 was 3.88 per cent, while the increase in the same period in the total realty value as computed from land sales was 4.20 per cent.

But it is generally conceded that probate court appraisals of real estate do not ordinarily reflect the full true value of the lands appraised. In Wisconsin two lines of investigation were followed for the purpose of determining to what extent on the average probate appraisals understate the true value of real estate. The question was put directly in a letter addressed to the various county judges and was answered by the judges of twenty-eight counties—not entire the *same* twenty-eight counties, however, before referred to. It was the concensus of opinion of these twenty-eight judges, each presumably having special knowledge of the subject in his own county, that ordinary probate appraisals of real estate represent 85 per cent of true value. In four Wisconsin counties a special investigation was made based on actual sales of parcels of land appraised in probate court. Only such sales were taken into account as appeared to have been made under normal conditions and which occurred within one year of the date of appraisal. In Dane county thirty-nine parcels appraised at a total of $179,219 were actually sold within a year of the appraisals at $220,151, the ratio of appraised value to selling value being only 81.41 per cent. In Fond du Lac county twenty-three parcels appraised at $109,935 were sold within a year at $124,355. the ratio of appraised value to selling value being 88.41 per cent. In St. Croix county and Winnebago county the ratios of appraised value to selling value were found to be, respectively, 85.37 per cent and 84.89 per cent. The average ratio for the four counties just named was 85.02 per cent—a ratio practically identical with that fixed by the opinions of the probate judges of twenty-eight counties, namely 85 per cent.

We stated earlier that the total value of taxable realty in twenty-eight Wisconsin counties in the year 1904 would have been fixed by probate appraisers at approxi-

mately $844,000,000. On the strength of the special investigations just described we assume that these $844,000,000 represented only 85.02 per cent of the full true value. If so the total true value of taxable realty in the counties in question, as computed from probate data only, was about $992,500,000 as against a total true value, as computed from land sales only, of a little more than $951,000,000. The two results vary by only 4.34 per cent. For the year 1905 the total true realty value for the counties in question, as computed solely upon the probate data, was a little over $1,031,000,000, as against a total of something over $992,000,000, as computed from land sales data alone. For 1905 the two aggregates vary by only 4.03 per cent.

In Minnesota investigations made as to the city of St. Paul still further demonstrate how strikingly real estate valuations worked out upon the basis of land sales are corroborated by results based upon probate appraisals.

In 1905 St. Paul real estate conveyed by warranty deeds for an aggregate stated consideration of $5,185,732 was assessed for taxation that year at $3,123,078, or at 60.22 per cent of its selling or true value. The total assessed value of all taxable real estate in St. Paul in 1905 was $75,191,692. Therefore, in accordance with the formula of the Wisconsin tax commission, the total true value of taxable real estate in St. Paul in 1905, on the basis of land sales, was $124,861,660.

In 1906 St. Paul real estate which was conveyed by warranty deeds for a total stated consideration of $5,516,552 was assessed for taxation at $3,228,467, or at only 58.52 per cent of its selling value. Dividing this ratio into the total assessed value of all St. Paul real estate in 1906 (being $79,398,227) gives as the total true value thereof $135,677,700, or an increase of 8.66 per cent over 1905.

In 1907 to September 1st only St. Paul real estate conveyed by warranty deeds for a total stated consideration

of $1,526,468, was assessed for taxation at $821,042, or at only 53.79 per cent of the selling value. This ratio divided into the 1907 total assessed value of all St. Paul taxable real estate ($82,137,007) gives as the total true value the sum of $152,699,400, or an increase of 12.54 per cent over the total for 1906.

In 1905 two hundred and twenty-five parcels of St. Paul real estate, which were appraised in probate court for a total of $305,580, were assessed at $214.896, or at 70.32 per cent of the appraised value. Dividing this ratio into the total assessed value of real estate for that year ($75,191,692) we reach $106,927,900 as the approximate sum at which the total value of St. Paul taxable real estate would have been fixed by probate appraisers in 1905.

In 1906 two hundred and forty-three parcels of St. Paul real estate appraised in probate court at a total of $318,595 were assessed at $224,925, or at a ratio of 70.60 per cent. This ratio divided into the total real estate assessment of 1906 ($79,398,227) produces $112,462,700 as the estimated total amount at which all taxable real estate in St. Paul would have been appraised in probate court in 1906. This sum exceeds the coresponding total for the year 1905 by 5.18 per cent.

During the first nine months of 1907 two hundred and three parcels of St. Paul real estate were appraised in probate court at a total of $250,770. They were assessed at $169,749 or at 67.69 per cent of their appraised value. The total assessed value of all St. Paul real estate in 1907 ($82.137,007) when divided by this ratio gives $121,342,900 as the estimated total at which all St. Paul taxable realty would have been appraised in probate court in 1907. The increase over the corresponding total for 1906 is 7.89 per cent.

Special investigation was also made in St. Paul to ascertain the amount of undervaluation prevailing in pro-

bate appraisals of real estate. Fifty-eight parcels which were appraised at a total of $100,360 were sold under apparently normal conditions and within a year of the respective dates of appraisal for a total consideration of $118,135. The appraised value bore a ratio of 84.95 per cent to the selling value. It will be noted that this ratio is substantially identical with the ratio which was found to prevail in the four Wisconsin counties.

We computed that the total value of St. Paul real estate would have been fixed by probate appraisers in 1905 at $106,927,900. If we assume that this sum is in fact only 84.95 per cent of the total true value then we arrive at the conclusion, based upon probate data only, that in 1905 the total true value of St. Paul taxable realty was $125,871,600. Its total true value for that year as above worked out on the basis of land sales only was $124,861,660. The result based on probate data varies from that based on land sales by less than 1 per cent.

In 1906 we find that the total true value of St. Paul taxable realty as worked out upon the probate data alone was $132,387,000 as against a true value of $135.677,770, as worked out from land sales only. The land sales value varies from the probate value by less than 3 per cent.

In 1907 the total true value of St. Paul taxable realty as computed on the basis of probate data only is found to be $142.840,400, as against a total of $152,699,400 derived from the use of land sales only. The aggregate based on land sales varies from that based on probate data by about 7 per cent.

Thus we have seen that both in Wisconsin and in Minnesota, there is substantial agreement of aggregate real estate valuations worked out by the use of land sales only with similar aggregate valuations worked out by the use of probate data only. This fact is one of very

great significance. The controlling facts on which real estate valuations are computed by the use of probate data are entirely distinct from the controlling facts which determine such valuations when worked out from land sales. There is no reason why results worked out upon one basis should not differ very widely and very erratically from results worked out upon the other except the fact that each process is well calculated to give results approximating the truth in a general way. But, as we have already shown, realty values as worked out by these two entirely different processes show a truly remarkable agreement one with the other. Each process thus lends credit and support to the other. It is no mere series of coincidences that year after year results substantially identical are reached by processes radically unlike. When two entirely independent lines of investigation, each prima facia well calculated to disclose the approximate truth, lead to substantially identical results, there is sufficient logical and scientific justification for the adoption of such results as an expression of the essential truth concerning the matter under investigation.

For more than four years now a large portion of my time has been spent in studying and analyzing the statistics of land sales. The greater part of this work has been done in connection with Wisconsin land sales, although I have also devoted considerable time to the study of such data in Nebraska, Minnesota, Iowa and South Dakota. I was very early convinced by such study and my later investigations have strengthened the conviction that land sales when properly gathered and intelligently used constitute the most practicable and most reliable basis thus far made use of, for the determination of the true aggregate real estate valuations of towns, villages, cities, counties and states and for the proper equalization of such real estate valuations between the various assessment districts and between the several

counties of a State. A reasonably careful study of the question will, I believe, lead most candid-minded men to a similar conclusion. Such study alone can enable any man to form an intelligent judgment concerning the subject.

The extent to which and the methods by which land sales can be properly used by local assessors in the work of endeavoring to assign equitable valuations to individual descriptions of real estate are matters of great importance. Many who admit the accuracy of the land sales basis for the determination of the aggregate realty values of whole assessment districts or counties are not as yet convinced that it can be safely employed by the local assessor as an aid in the performance of his work.

During the present year I have spent much time in search of a feasible and reasonably accurate method by which local assessors may make use of land sales. This investigation has thus far been based solely on recent land sales in the city of St. Paul. Before proceeding to a detailed description of the process finally settled upon it will be well to call attention to the remarkable manner in which results worked out by use of the process are corroborated by the concensus of opinion of a considerable number of the leading real estate experts of the city of St. Paul.

The process, so far as city property is concerned, is directed to the ascertainment of the correct average ground value per front foot in a given year for a distance of one block along a given street. By the term "ground value" is meant the value of the land alone, exclusive of the buildings thereon. A residence district in the western part of the city was selected as the territory within which to compare ground values worked out by this process with ground values as established by expert opinion. This district, which comprises over 300 platted blocks, extends from Western avenue on the east to

Cleveland avenue on the west (a distance of 3½ miles) and from Marshall avenue on the north to Osceola avenue on the south (a distance of nearly one mile). It is the residence district in which there has been the greatest activity in real estate during the past three years, and every leading real estate dealer in the city is entirely familiar with present ground values in at least a considerable number of localities within the district. The lots within the district vary in value from a dollar a front foot to over one hundred dollars per foot. In some portions of the district most of the lots have buildings on them; in other portions all or nearly all of the lots are vacant. In some localities within the district values have increased very rapidly during the past three years, while in others they have advanced very little or not at all.

Average ground values per front foot for the year 1907 were computed by use of the process for 277 separate localities within the district, each such locality being for the distance of one block along a given street, as, for instance, on Summit avenue, from Dale street to St. Albans street. As to each of these 277 different localities the opinions of real estate experts were gathered in writing. From four to ten such opinions were gathered and collated as to each locality or block.

For the purposes of comparison the 277 blocks were classified in four groups: First, those blocks in which the average ground value was less than $10 per front foot; second, those in which it ranged from $10 to $20 per foot; third, those in which it ranged from $20 to $40 per foot; and fourth, those in which it exceeded $40 per foot. For the ninety-six blocks which fell in the first group the average value fixed by the land sales process was $6.15 per front foot as against an average value of $6.70 per front foot as fixed by the concensus of expert opinion. The variation between the two was 55 cents

per front foot or $22 per lot on lots averaging about $250 in value.

For the sixty-nine blocks in the second group, the average value as computed by the process was $14.10 per front foot as against $15.45 per front foot as fixed by the experts. The difference was $1.35 per foot or a little over $50 per lot on lots of an average value of about $600 each. It should be noted that this group includes considerable territory in which the recent rate of increase in value has been unusually, if not abnormally. rapid.

For the eighty-two blocks in the third group, the average value as fixed by the land sales process was $28.55 per front foot as against $29.55 per foot as fixed by the experts. The variation between the two was one dollar a foot or $40 per lot on lots worth between $1,100 and $1,200 each.

For the thirty blocks in the fourth group the average value as fixed by the process in question was $63.10 per front foot as against $63.20, as fixed by the experts, the two averages being practically identical.

Treating the entire 277 blocks as a unit, the average ground value per front foot in 1907, as determined by the land sales process, was $20.95 as against $21.75, as fixed by the concensus of expert opinions. The variation between the two was less than 4 per cent or only 80 cents per front foot and amounted to only $32 per lot on lots of an average value of between $800 and $900 each.

The ground values computed by use of the process when compared with those fixed by the experts for blocks fronting on Lincoln avenue (one of the representative residence streets in the district) will still further illustrate in a more concrete manner the close agreement existing between values derived by use of the two different methods.

	Average Ground Value per Front Foot		
	Land Sales	Experts	
	Process	No. of	
Lincoln Avenue—	Dollars	Experts	Dollars
Dale to St. Albans	$47.00	7	$50.85
St. Albans to Grotto	49.00	8	51.20
Grotto to Avon	49.00	8	51.80
Avon to Victoria	50.00	9	51.65
Victoria to Milton	35.75	7	36.05
Milton to Chatsworth	29.00	8	29.85
Chatsworth to Oxford	27.50	8	26.55
Oxford to Lexington	24 00	7	24.20
Lexington to Dunlap	15.00	7	16.45
Dunlap to Griggs	12.00	7	12.20
Griggs to Syndicate	8.50	7	8.90
Syndicate to Hamline	8.50	7	9.35
Hamline to Albert	7.00	7	8.05
Albert to Pascal	7.00	7	7.95
Pascal to Saratoga	5.00	6	6.40
Saratoga to Snelling	5.00	5	5.90
Macalester to Cambridge	9.00	6	9.35
Cambridge to Baldwin	9.00	5	9.20
Baldwin to Fairview	9.00	5	9.20
Fairview to Prior	3.50	5	3.90
Prior to Cleveland	3.50	5	4.10
Average for 21 blocks	19.75	7	20.60

We will now describe the process by which land sales were used in working out the ground values per front foot in the residence district in St. Paul before mentioned.

The sales of St. Paul real estate made by warranty deeds only, between January 1, 1905, and September 1, 1907, were gathered from the public records in the register of deeds' office. Only such sales as were apparently normal in character were used. These sales were transcribed upon cards printed and ruled for that purpose. The cards are 4x6 inches in size. They are ruled with suitable columns for the date of the transfer, name of grantor, volume and page where recorded, description, consideration stated in the transfer, total assessed value, and assessed value of improvements. There is space on each card below the headings for eleven items or transfers. A seperate card is devoted to the transfers in

each individual block, the name of the addition and the number of the block being written in the blank space at the top of each card. These cards are filed in a card index cabinet, alphabetically with respect to the several additions and numerically with respect to the blocks in each addition. When the transfers in a given block become too numerous for a single card, a second card is added and so on. It is an easy matter to produce instantly the card or cards containing the recent land sales within any given block in the city.

All the information as to land sales shown on the cards comes from the recorded deeds except that concerning the assessed value of the several parcels conveyed. The latter information as to each item is posted to the card from the assessment roll for the year in which the transfer occurred.

I have also entered probate appraisals of lots in a given block on the same card with the land sales, the probate entries being made in red ink to distinguish them from sales. The assessed values of such appraised parcels are also filled in from the proper assessment rolls.

We will assume that the land sales and probate appraisals have all been gathered and properly entered on the cards, together with the assessed valuations of the several parcels and that it is proposed now to work out from this information the ground value of lots situated in a given addition. In order that the method may be more clearly understood I will describe the manner in which I made use of it in what is known as Anna E. Ramsey's Addition. That addition has been developing rapidly during the past three years. A considerable part of the property transferred has been improved property, though the greater portion has been unimproved.

In other sections of the city of St. Paul (as would also be the case in many districts of other cities) most of the sales which take place are sales of improved

property. In order that such sales may be used in determining average ground values along given streets it is apparent that some method must be devised by which to estimate what portion of the total consideration stated in a group of deeds was represented by the value of the ground and what portion by the value of the buildings thereon. In eight different blocks located in various portions of Anna E. Ramsey Addition both improved and unimproved property, has been sold since January 1, 1905. Taking the unimproved property in these eight blocks by itself, we find that vacant lots which were sold for an aggregate consideration of $42,950 were assessed at a total of $25,250, or at 58.94 per cent of their true value. Then taking up the sales of improved property in these same eight blocks we find that the total assessed value of the ground transferred by such sales was $3,910, which is taken as representing only 58.84 per cent of its true value—the ratio of assessed to true value found for vacant lots in the same blocks. The estimated true value of the ground alone transferred by these sales of improved lots is $6,645. Deduct this from the total consideration paid for such improved property, including the buildings, namely $63,950, and we have left $57,305 as the approximate amount for which the buildings on the improved property were sold. They were assessed at an aggregate of $22,025, or at 38.44 per cent of their selling value. (I may say in passing that similar calculations made from land sales in various widely separated additons in St. Paul have led me to the conclusion that as a whole buildings in that city are assessed at present at an average of about 40 per cent of their actual value).

In order that land sales running back any considerable period of time (say three years or longer) may be accurately used in working out present ground values it is necessary to know whether such values are increasing

or decreasing in a given district and the approximate rate of increase or decrease. I will now explain how this particular problem was worked out in Anna E. Ramsey Addition. During the two years 1905 and 1906 unimproved lots in that addition which were sold for $105,-241 were assessed at $51,530, or at 48.96 per cent of true value. All lots in the addition (exclusive of the buildings) were assessed for those two years at an average of $231.515. This sum, divided by the ratio 48.96 per cent just stated, gives as the estimated average ground value of the entire addition for the two years 1905 and 1906 the sum of $472.870. During the year 1906 and to September 1, 1907, the total consideration paid for unimproved lots sold in this addition was $61,834, the total assessed value against the same being $28,045, or only 45.35 per cent of the selling price. This ratio divided into the total assessed value of all lots in the addition (exclusive of buildings) in 1906 and 1907, namely $229,735, gives as the approximate average true ground value of all lots in the addition for the years 1906 and 1907. the sum of $506,580, as against a total average value for the two years 1905 and 1906 of $472,870. The later two year period shows an increase of 7.13 per cent over the earlier period; in other words, as indicated by an analysis of the sales of the last three years, the average ground value of lots in Anna E. Ramsey Addition has advanced at a rate of about 7 per cent per annum.

We are now ready to make the computations of average ground value per front foot for a specific locality in Anna E. Ramsey Addition. As an illustration let us compute such average value for the single block along Dayton avenue from Griggs street to Syndicate street. The particular two blocks which front on Dayton avenue between Griggs and Syndicate are block 3 on the north side of the avenue and block 6 on the south side. We use the land sales and appraisals made during the past

three years in each of these blocks and also in the blocks immediately adjoining for a distance of one block in either direction on Dayton avenue; that is, blocks 2, 3 and 4 on the north side of the avenue and blocks 5, 6 and 7 on the south side. During the three years the total value of Dayton avenue frontage sold in these six blocks as fixed by the deeds was $24,925. The assessed value of the buildings located on the improved lots thus sold was $4,600. This assessed value of the buildings is assumed (on the strength of the special calculations before referred to) to represent only 38.44 per cent of true value. On this basis the true value of the buildings included in such sales was $11,970, which, deducted from the total consideration paid for all property sold in the six blocks ($24.925) leaves as the amount received for the ground alone the sum of $12,955. The total Dayton avenue frontage conveyed during the three years in the six blocks was 1,020 feet. This, divided into $12,955, gives $12.70 as the average selling price per front foot during these three years ending in 1907 of the Dayton avenue lots located in these six blocks. The center of this period is 1906. We desire to know, however, the ground value in the year 1907. We have already shown that the average rate of increase in ground value in this addition during the past three years was 7 per cent per annum. We, therefore, increase the average ground value per front foot for these six blocks for a three-year period, of which 1906 is the center year, by 7 per cent in order to express the full value in the year 1907. This gives us $13.60 per front foot as the average value in 1907 of the Dayton avenue lots in the two center blocks, namely, blocks 3 and 6. The average value fixed for the same by the concensus of opinion of nine experts was $13.90 per front foot.

In a similar manner was worked out each of the 277 average values per front foot in the residence district

in the western part of the city of St. Paul. In a few localities, owing to special conditions, the sales in only two blocks on each side of the street were taken as the basis of calculation, but in most instances the sales from six blocks, three on each side of the street, were used. Attention should again be called to the striking manner in which the ground values worked out by this process are confirmed by the opinions of well-qualified experts. In the ninety-six blocks in which the average value per front foot was less than $10 there were only seven instances in which the value determined by the process varied as much as $1.25 per foot or $50 per lot from the average value fixed by the experts. In the sixty-nine blocks which ranged in value from $10 to $20 per front foot there were fourteen blocks only in which the variation amounted to as much as $2.50 per front foot, or $100 per lot. In the eighty-two blocks in which the value ranged from $20 to $40 per front foot there were only fourteen blocks in which the variation amounted to as much as $3.75 per foot, or $150 per lot. In the thirty blocks in which the average value per foot exceeded $40 there were only five blocks in which the variation exceeded $5.00 per foot, or $200 per lot.

The process that has been described is not put forth with any claim that it is perfect. It is submitted for the careful consideration of that portion of the public having an intelligent interest in such subjects, with the hope that it will be found to contain suggestions which are helpful. I deny the competency of any person to state, without first having made a thorough and a candid investigation, that the process is not, in its essential features, well calculated to solve, with approximate correctness in most localities and under most conditions, the problem which it was designed to solve. It is not a mere untested hypothesis. It has been submitted to a comprehensive and a thorough test and has not been found wanting.

On the contrary, it has been found by the best qualified experts to produce results which, as a whole, are surprisingly accurate, and are so considered and so conceded by the experts themselves. A process which has successfully responded to such a test is surely entitled to something more than a mere fleeting interest on the part of all who are concerned in the valuation of real estate for purposes of taxation. If the process is imperfect, as no doubt it is, let us ascertain by practical tests wherein it is imperfect and seek a proper remedy. If it needs to be modified in various respects in order to be safely employed in a given locality let the proper modifications be devised to suit the particular conditions and the process then put to use.

Within the limits of the present paper it is impossible to explain the process with all that fullness of detail and illustration which is perhaps necessary to a perfectly clear understanding of the matter. For this reason I shall be pleased at any time to give such further information as may be desired concerning any features of the process not clearly understood.

Just a word as to the time and expense necessarily involved in working out ground values by the process described: It is my judgment, based on my own experience and observation, that in cities of the size of St. Paul and Minneapolis, two men, who are familiar with the city at large and with the public records, who are reasonably proficient in the handling of ordinary arithmetical problems and who are also willing (even though engaged in the public service) to do a reasonable day's work for a reasonable day's salary the year around will be an adequate force for the compilation of the land sales and other significant data, and for the computation therefrom, *every year,* of reasonably accurate ground values per front foot for nine-tenths of the entire taxable area of the city.

A process which has been successfully put to use in determining ground values in a residence district comprising about 7 per cent of the entire area of St. Paul can surely be used with like success in determining such values in at least all other *residence* districts of that city. If it can be thus used in St. Paul, why can it not be used in any other city and in every other city? If it can be used in cities for the determination of average ground values per front foot in a given block along a given street, why, with proper modifications, can it not be used for the determination of average value per acre in a given government section in the country?

VALUATION OF REAL ESTATE BY THE WISCONSIN TAX COMMISSION.

By Thos S. Adams.

When in the year 1901 the legislature of Wisconsin transferred from an old-fashioned board of equalization, composed of the governor, secretary of state and state treasurer, to the newly-created tax commission the duty of equalizing county assessments (or making the state assessment, as it is called in Wisconsin), the tax commission, to use a classic Wisconsin expression, "seen their duty and done it." The old board had been comfortably equalizing property for some years on a basis actually lower than the aggregate local assessment. Between 1894 and 1900, for instance, the aggregate local assessment had risen from $632,707,113 to $746,022,932, while the state assessment had risen from $600,000,000 to $630,000,000, notwithstanding the fact that the law required the State board of assessment (as the state board of equalization is called in Wisconsin) to assess property at full value according to their best judgment. The tax commission, however, refused to temporize, and took the law at its word. The state assessment, which had been $630,000,000 in 1900, was raised to $1,436,284,000 in 1901, an increase of 128 per cent.

This simple acceptance and honest execution of their legal duty made some trouble. There were permanent state appropriations fixed at so many mills per dollar of assessed valuation, which were enormously swelled by the assessment of state property at something approaching full value. The state school tax "of one mill for each dollar of the assessed valuation" was suddenly in-

creased from $630,000 in 1900 to $1,436,284 in 1901, and many school districts received more money than they knew what to do with wisely. But the tax commission having announced in advance that they would actually assess the property of the State at full value, as the law directed them so to do, and having pointed out the effect of full valuation upon the school taxes, did not hesitate to carry out their convictions when, despite their warning, they were saddled with the duty of making the state assessment.

The spirit displayed by the tax commission in their first state assessment has animated their subsequent work. Since 1901 the total valuation of the property of the State has been steadily raised from $1,436.284,000 to $2,256,300,000. The valuation of real estate similarly has been increased from $1,186,349,139 in 1901. to $1,780,265,161 in 1907. This careful and efficient performance of the first important administrative task laid upon them has naturally brought increased power and expanded jurisdiction. In 1903 the adoption of the ad valorem tax on railroads gave to the state assessment new meaning and importance. According to this law, railroads must be taxed at the average rate of taxation borne by the general property of the State. More specifically the rate of taxation paid by the railroads is ascertained by dividing all the property taxes collected throughout the State by the true value of property as determined in the state assessment. The importance of the latter, then, is no longer a mere matter of relative county burdens. It is not sufficient that the proportion of the state assessment assigned to each county shall be correct. The absolute or total valuation must be correct in justice to the railroads and the people, because it is plain that as the state assessment goes up or down the tax upon the railroads goes down or up. Finally, in the year 1905 the tax commission was empowered to settle disputed county equal-

izations; and they are now, to cite a timely example, re-equalizing the assessments in Monroe and Racine counties. To decide these appeals intelligently it is necessary that the tax commission shall not only have the county valuaions accurately determined, but that, in addition, they shall have some fairly accurate idea of intra-county values, of the relative taxable importance of the several assessment districts within each county.

The magnitude of this task of assessing accurately all the property in the State in such a way that the commission shall obtain accurate results for each of the seventy-one counties, and fairly accurate results for each of the 1,500 odd assessment districts, is somewhat overpowering. Evidently, it can only be worked out by some more or less mechanical system. The operation and character of this system, as applied to real estate only, is the specific topic with which I shall occupy myself during the remainder of my time.

The method of valuation, in brief, is the so-called "sales method." As early as 1873, a far-sighted legislator, Mr. F. W. von Cotzhausen, secured the passage of a statute directing registers of deeds to return annually to the proper county clerks and to the secretary of state a complete record of all the bona fide sales made within their respective counties, showing for each sale, in addition to the description and other data, the price at which the property was sold and the assessed value of the same property on the last tax roll filed with the county clerk. It is the information contained in these reports which has enabled the Wisconsin tax commission, sitting as a state board of assessment, to make what must be numbered among the best state equalizations of real estate assessments made in this country. During the last three years, it may be added, the tax commission has subjected a majority of the registers' reports to the closest scrutiny and revision; and in the legislative

session of this year a new statute was passed providing for the direct collection of statistics of sales by special agents of the tax commission.

The exact process by which the sales method is applied requires no lengthy description. Each sale is accompanied by two valuations—the selling price or consideration and the assessed value. The sales for each assessment district are tabulated separately; considerations and assessments are added and a ratio of true to assessed valuation secured. This ratio is then applied to the total assessment of the district, with the result that the latter is raised in the same proportion that the aggregate price exceeds the aggregate assessed value of the property sold. The result is known as the annual true value. The process just described is repeated for the five most recent years for which statistics can be obtained, and the average of the five annual true values is usually accepted by the tax commission as their estimate of the true value of real estate in the assessment district in question. I say "usually accepted by the tax commission," because the commissioners do not attach any sanctity to the method under discussion, and if it yields results which are palpably and plainly inconsistent, they modify such results according to their best information. The sales do not in the opinion of the commission determine values; they supply evidence which assists the commission in determining values. The judgment of the commission, acting upon all the evidence, is always the court of last resort. However, it is, I think, correct to say that the sales method is followed in a very large majority of counties and assessment districts.

The tax commissioners of Wisconsin, then, are evidently satisfied that the sales method offers, in a large majority of cases, a practical and fairly accurate process of estimating the true value of real estate. After a rather intimate study of the method for about four years,

I find myself more and more convinced of its substantial accuracy. The remainder of the paper will be devoted to a consideration of its strength and weakness, in the hope that other States which are considering the introduction or wider use of the sales method may find something of value in the unusually extensive Wisconsin experience.

In considering the topic it will probably prove most helpful to discuss *seriatim* the principal criticisms which have been directed from time to time against the sales method.

I. INACCURATE DATA

The criticism most commonly launched against the sales method is that a large amount of erroneous data is likely to creep in, that nominal sales at fanciful or fictitious prices, trades, quit claims and other unsuitable items of similar character are likely to occur in such quantities as to vitiate the results.

The answer to this objection is threefold: (A) that the accuracy of the data will of course depend upon the care with which it is collected; (B) that with only a reasonable amount of precaution, an amount which can be taken without prohibitory expense, the results for counties and the large assessment districts will be substantially correct; (C) and that with practically no care or precaution at all, the results in a large majority of instances will be surprisingly near the truth. Let us consider these statements in order.

(A) The definition of a "good sale" for the purpose in hand is not altogether simple and easy. but the standard or test may be briefly stated as follows: In an acceptable or good sale (1) a full title will be passed, (2) the assessment will apply to precisely the same property sold, (3) the conditions of the sale will not be indisputably and unmistakably abnormal, (4) and the com-

plete or net price of the real estate will be stated in money or in terms easily and safely convertible into money.

(1) Because a full title is not necessarily passed, and because, moreover, the transfers often do not represent "cash sales in the ordinary course of business," it is necessary to exclude sheriffs' sales, foreclosures, administrators', executors', trustees', guardians', referees', receivers' and assignees' deeds, quitclaims and a variety of similar conveyances in which the title may not be fully warranted. Occasionally an executor's or guardian's deed, or even a quitclaim may be used, after careful examination, but in a large majority of such cases it will be found that the transaction is nominal, for the purpose of settling an estate, for example, or that the price is noticeably affected by the conditions which prevented the use of a warranty deed. Executors frequently assure us that they received the full market price, that the sale was perfectly representative and suitable for our purpose, but frequent comparisons of such executor's sales with ordinary sales in the same district have convinced us that such a statement is seldom exactly true. In the long run even the most carefully selected executor's and guardian's deeds will show a higher ratio of assessed to true value than a group of ordinary sales from the same district.

(2) Because the assessment does not apply to the property sold it is necessary to exclude payments in fulfillment of land contracts, sales in which a large amount of personalty figures, and cases in which buildings were erected or destroyed between the assessment and the sale. All these are important sources of error and require some comment.

I see no adequate reason for excluding land contracts if they can be employed in the year in which the contract was made; but naturally the last payment which usually

accompanies the formal transfer of the title is not an adequate measure of the value of the property, because it is likely to be a partial payment, and moreover, when it is a full payment, it represents the value of the property at some earlier date. It may be worth while to add that it is often possible to detect a transfer in fulfillment of a land contract from the wording of the deed and the tax roll. If the warranty clause excepts "taxes since 1903" and the rolls show that the grantee has been paying the taxes since 1903, the transfer is practically always in fulfillment of a land contract of that date.

Sales in which a small amount of personalty figures may safely be corrected by subtracting the value of the personalty, which ordinarily can be learned by visiting or writing the parties to the sale. But where the personalty approaches or exceeds in value 20 per cent of the consideration, correction is exceedingly difficult, and unless data are scare, the sale should be discarded. I may add that, in Wisconsin at least, the proportion of cases in which personalty figures is surprisingly small, and the error from this source is much smaller than the average man supposes. In a very large majority of cases the consideration stated in the deed applies to the real property alone, and in a large proportion of the remaining cases some reference to the personalty is made in the deed.

The last class of sales included in the group which we are now discussing, comprehends cases in which property was erected or destroyed between the time of assessment and the time of the sale. Such cases are not numerous and not important, although (as might be expected) the number of cases in which buildings are added greatly exceeds the number in which buildings are taken away or destroyed. Cases of this kind can usually be detected in Wisconsin by examining the assessment of the improvements before and after the sale. If a city

lot, for example, is assessed for $600 in May 1904 with nothing for improvements, sold for $3,000 in December, 1904, and assessed $2000 on improvements in May 1905, there is pretty strong evidence that a building was erected between the earlier assessment and the sale. Such cases, accordingly, are seldom passed over without writing or interviewing the parties to the sale. They fly, as it were, an unmistakable danger signal, in the wide discrepancy between assessment and consideration.

On the other hand there is a subtler change which is more dangerous, the impalpable advance or fall of real estate values which is almost always taking place. This constant flux of values makes it advisable that the year or time unit should be so selected that the assessment period will fall at its center. There should be, for obvious reasons, as many sales after as before the assessment. In Wisconsin, for test purpose, we have arranged our sales in two ways. In the first, all sales are compared with an assessment completed before any of the sales were made. In the second, the year is arranged so that the assessment period falls practically in the middle of the sales. We call the first the "Preceding Year Comparison," the second the "Calendar Year Comparison." Last year the "P. Y. Comparison" yielded true values 3.67 per cent in excess of the "C. Y. Comparison." There is only one danger in the method of placing the assessment in the middle of the sales. Occasionally, an assessor goes over the records of deeds and raises the assessments of those properties which have been sold. Of course where this is done, the assessed value of property sold before the assessment is much nearer its true value than is the case with other property in the district. But it is very easy to detect this practice where it occurs, and to make allowances for it.

(3) The third requirement of a good sale as noted in in the definition is that the conditions of the sale must not

be indisputably and unmistakably abnormal. I phrase the condition in this way because people differ so radically concerning what is abnormal, that a sale should not be excluded on this ground unless there is practical unanimity of option concerning its unsuitableness. Sales to the government, particularly to municipal governments, are plainly precluded because of the excessive price which is almost always paid. Sales to railroad companies fall under the same ban; nobody denies, I suppose, that the railroads are systematically and outrageously held up. On the other hand when we come to sales to breweries for saloon purposes, to farmers paying fancy prices for adjoining fields or right of way which is worth more to them than anybody else. and to the so-called "forced sales," we have reached very debateable ground. Sales of this sort should ordinarily be included in the computation, because of the strong likelihood that the case in which an excessive price was paid will be balanced by those in which the owner was forced to accept an inadequate return, and because there is no sure criterion of what constitutes exceptional and abnormal circumstances. Long experience in this work has convinced me that buyers of real estate are divisible into two great classes; the class of those who are sure they have "done" the other fellow, and the pessimists who are equally sure that the other fellow has "done" them. In a specially close and careful study of 15743 sales which I made at one time, primarily to test methods and processes, only twenty transfers were thrown out on the ground that they were "forced sales" of such indisputable character that their inclusion was plainly impossible. In concluding this brief discussion of abnormal sales, I desire to call attention to the fact that it is not legitimate to exclude every sale which deviates markedly from what appears to be the general ratio between assessed and true values. In every assessment district there are some ex-

ceedingly low and some exceedingly high assessments. Now when one of these unusual cases appears among the data, it is not to be excluded simply because it deviates from the general run of things. The peculiar sale is needed to represent the peculiar assessments. Of course if there is reason to believe that these exceptional cases occur more frequently among the sales than among the assessments, there is good reason for debarring it. This, for instance, is the case with city purchases which are always recorded with the exact consideration, whereas a large proportion of ordinary deeds state the price as "$1 and other valuable considerations." But in general, and particularly when a five-year average is being employed, a transfer should not be debarred merely because the assessment is unusually high or low in proportion to the price.

(4) The final condition of the definition is that the true or full price of the property must be stated in money or in terms easily and safely convertible into money. Because of their violation of this canon we exclude trades, nominal sales of many kinds, sales to relatives, transfers affected by material reservations and restrictions, transfers in which the consideration is fictitiously misstated, and transfers in which the consideration stated in the deed must be increased by mortgages, back taxes or other liens of unknown amounts. The defective sales included in this class are important and might profitably be discussed at some length. I confine myself, however, to these relevant considerations: (a) Sales to relatives are almost always wrong and misleading. In hundreds of sales between brothers, particularly, we have been assured by the parties that the relationship made no difference in the price. But in the long run, inevitably, and in a large majority of the individual cases, the ratio in such sales will be higher (i. e. the assessed value will be nearer the sale value) than in the other sales of the

district; so that I have been forced to conclude that relationship often causes the price to be shaded when the parties themselves are unconscious of the fact. (b) Building and liquor restrictions seldom affect the value of property adversely, so that it is safe to disregard such restrictions when they are mentioned in the deed. (c) In thousands of transfers a mortgage is assumed by the grantee, but the language of the instrument leaves one in doubt whether the consideration stated is inclusive or exclusive of the mortgage. Our experience in Wisconsin shows that the mortgage should be added to the consideration stated in the deed in only a very small percentage of the cases. Out of 1414 good sales in which a mortgage was assumed by the grantee, careful investigation revealed the fact that in only 6.1 per cent of the cases was it necessary to add the mortgage in order to get the full price, and this percentage was increased by an abnormally large number in one of the five counties specially investigated. In the average county the percentage of "added mortgages" will be less than this. The omission of the mortgages in these cases cause, or would have caused had the mortgager not been properly added, an error of less than 1½ per cent among the mortgage cases alone, and spread over all the sales the effect of the omission would have been negligible. The ratio of assessed to true value for the 1414 sales omitting the mortgages was 49.85 per cent; adding them the correct ratio of assessed to true value was 48.54 per cent.

(B) In the preceding discussion I have tried to define by exclusion the kind of sales that may properly be used in estimating the true value of real estate. I now take up the proposition that with a reasonable amount of precaution, an amount that can be taken without prohibitory expense, data can be obtained which for counties and the larger assessment districts will yield correct results. In Wisconsin we divide this work of collecting

data of sales into two parts—"office work" and "field work"—the former including the examination of deeds and assessments at the county seat, the latter covering the examination of the parties to the sales and the verification of the office results in the field. Now the point which I am making is simply this: if the office work is carefully done, field work in general is unnecessary.

The jutification of this statement is found in the fortunate circumstance that the errors which remain after office work is finished and which can only be eliminated by actual interviews with the parties to the sales, are in an unusual and striking degree compensatory. In the first investigation made for the Wisconsin tax commission, covering four counties (including the City of Milwaukee) and involving the most thorough investigation of nearly 16000 sales, special study was made of the influence and occurrence of the various kinds of errors. It was ascertained that the most important classes of erroneous sales which field work brings to light are: trades and old land contracts; transfers including some personal property and cases in which the mortgage should be added to the consideration stated in the deed; cases in which buildings have been added or destroyed between the assessment and the sale and sales to relatives; sales in which the purchaser has been deliberately misled concerning the character of the property and sales in which the consideration has been fictitiously misstated. I have enumerated these errors in couplets, each couplet consisting of an error which in the long run exaggerates and one which reduces the true value of the property. The result is that the net error is very small, practically negligible. Of course there are other kinds of field errors. For instance. mortgage loans recorded as ordinary transfers in order to avoid the old mortgage tax, were formerly common in three or four counties. But the other errors are very infrequent.

The compensatory character of "field errors" was shown very clearly in the first investigation which I conducted for the Wisconsin tax commission. In this investigation true values were computed from the sales as they stood at the completion of office work, and compared with the true values based upon the revised sales. The figures are given immediately below. The total true value after field work was $385,436,821. The total true value based upon office work alone was $385,737,536. The difference is less than one-tenth of one per cent. And the differences for the individual counties are not great. The greatest discrepancy was in Dane County where it amounted to less than 2 per cent. This discrepanacy in Dane, it may be added, was almost wholly due to the discovery in the field of a large number of old land contracts which, at that time, we had not learned to detect in the office work. Moreover, I may say, that this whole comparison is unfair to the possibilities of office work because during the first investigation we had not learned the significance of those signs and signals which to the experienced agent give warning of irregularity. Notwithstanding this inexperience, however, the results of the first investigation amply prove, what all our subsequent experience tends to confirm, that for nearly all counties, and for a large majority of assessment districts, field work accomplishes no material change in the results.

Comparison of Annual and Average True Values Based Upon Office Work with Similar True Values Corrected by Field Investigation.

Year	Barron County	Dane County	Milwaukee County	Ozaukee County	Four Counties
1899—					
Office & field.	$ 5,696,361	$55,204,576	$285,319,975	$11,611,955	$357,832,867
Office only...	5,113,915	55,776,079	285,468,400	11,824,090	358,182,484
1900—					
Office & field.	6,104,109	61,080,877	278,415,872	12,420,022	358,020,880
Office only...	5,907,298	59,007,353	281,469,458	18,913,410	359,297,519

Comparison of Annual and Average True Values Based Upon Office Work with Similar True Values Corrected by Field Investigation.

1901—					
Office & field.	8,050,495	67,159,762	302,556,804	14,224,552	391,991,613
Office only...	8,132,712	64,638,125	305,310,300	13,952,877	392,034,014
1902—					
Office & field.	9,814,282	71,672,481	300,811,143	14,189,906	396,487,812
Office only...	9,418,008	70,688,593	302,458,900	13,857,141	396,422,642
1903—					
Office & field.	12,119,829	78,137,486	317,330,814	15,262,790	422,850,919
Office only...	11,651,212	76,783,044	318,834,600	15,482,160	422,751,016
1899-1903—					
Office & field.	8,357,018	66,651,036	296,886,922	13,541,845	385,436,821
Office only...	8,044,629	65,378,639	298,708,332	13,605,936	385,737,536

I should say in fairness that field work sometimes, though relatively seldom, makes considerable difference in the value of particular assessment districts; and that a certain amount of it is always desirable if for no other reason than to develop the full possibilities of the office work. At the present time in Wisconsin we follow this procedure: If a complaint against the county equalization has been made or is likely to be made, we "field" the sales carefully, visiting the parties to the sales and inspecting the property if possible. If no appeal from the county equalization is probable, we confine the field work to districts in which sales are scant, although we always investigate by letter or schedule sales which appear abnormal and suspicious, particularly when such sales are large enough to exercise an appreciable effect upon the ratio. Where there is no reason for unusual care or precaution we "field" many sales with the notaries or conveyancers who have attested the deeds, with town clerks and real estate agents. Our usual practice is to test the knowledge and truthfulness of such persons by asking them about a conveyance or two which we have previously investigated. The intimate knowledge which such persons have of real estate transfers in rural districts is sur

prising, and in nineteen cases out of twenty they not only know the facts, but are willing to state them when they are informed what use is to be made of them. Quite recently I had occasion to go over carefully two important assessment districts which had been "fielded" originally with notaries and town clerks. Appeals against the county equalization had been taken to the tax commission and it was important that our data should be as perfect as possible. The result of the second canvass was two or three trifling changes out of about sixty sales, which changes made no appreciable difference in the original results. Experience shows that the careful "fielding" of dubious districts, added to a judicious mixture of written inquiries and visits to notaries and town officials, secures substantially exact results. so far as the sale method is capable of yielding such results.

(C) I have stated above that even with no particular care or precaution at all the results for most counties will be surprisingly accurate. Of course this is necessarily an indefinite assertion; the meaning of which can be illustrated better than it can be defined. Up to the present year these statistics of sales and corresponding assessments have been returned to us by the registers of deeds acting under instructions from the tax commission. On the whole these returns have been made rather carelessly, a few of them with something approaching criminal carelessness. Owing to the fact that the registers were paid so much per folio, they were under a strong temptation to pad their reports with sales which were plainly unsuitable. Our agents carefully revised the work of the registers in forty counties, but the estimates of true value based upon the revised returns differed from the estimates based upon the registers' returns by only 3.09 per cent. In seven counties the revised true values were less than the unrevised, but the difference in none of the seven counties was as high as 8 per cent. In sixteen coun-

ties the revised returns exceeded the unrevised by less than 3 per cent, in nine counties from 3 to 6 per cent, in two counties from 6 to 9 per cent, in three counties from 9 to 12 per cent, and in three counties over 12 per cent. The difference in one county was as high as 25.17 per cent. It was the possibility of differences as great as this in single counties which made it necessary to take this work away from the registers; although in the great majority of counties, despite gross carelessness, their reports yielded results not far removed from the truth. The explanation of this fact is found in the circumstance that they were merely careless, not biased; they were intent only upon increasing the body of data and not upon giving that data a particular twist or coloring.

II.—ARE THE SALES REPRESENTATIVE?

Up to this point I have been discussing the criticism that it is impossible or very difficult or very expensive to get accurate statistics of sales. I now wish to consider the far more specious charge, so frequently made, that the sales are not representative of the property. The sales method involves what statisticians call the process of "sampling." The criticism is that the samples are not fairly and evenly selected. My own conclusion, based not on *a priori* analysis (for when I began to study the subject I expected to find that the criticism had real weight) but upon rather extensive experience and study of the facts, is strongly to the effect that this charge has no practical foundation. And the reason why it possesses little practical significance is this: the fact that a given class of property, say suburban lots, is unduly represented in the sales, is of no importance unless this class of property is assessed at a markedly different proportion of true value than other classes of property. On the other hand the fact that a given class of property is assessed at a plainly unusual and abnormal proportion of true value

is of no significance unless this class is seriously misrepresented in the sales. Two conditions must combine and conspire to give force to this criticism—a special class of property must be abnormally assessed and at the same time be seriously misrepresented in the sales—and this combination of circumstances, over districts of any size, seldom occurs. And even when it does occur the resultant error is surprisingly small. If, to take an illustration, a given district is composed equally of urban and rural lands ("lots" and "lands" as we call them in Wisconsin), while the lots are assessed 10 per cent higher than the lands (which is much more than the actual average difference) and over-represented in the sales to the extent of 10 per cent (a fair example of misrepresentation) then the resultant error in the estimate of true value is something less than one-quarter of one per cent.

Moreover, the tabulation of data and computation of true values by assessment districts secure, in a rough way, a proper distribution of the sales. If, for example, large properties are under-represented in the sales and under-assessed relative to other property, these large properties are, in a rudely efficient way, segregated by the selection of so small a territorial unit as the average assessment district. Sales within this district only are used in computing the true value of the district, while the sales in other districts, relatively too numerous, exert no influence upon the value of the district dominated by the larger properties.

Of course, this use of the assessment district as the unit of tabulation would not wholly eliminate the error of which we are speaking, for several reasons. But it would partially counteract the defect of misrepresentation. What is more important, from the present standpoint, if there were serious misrepresentation in the sales, county values estimated by treating all the sales of the county together—the "unit method" we call it—would

differ seriously from the county values computed by adding togeher the true values of the assessment districts of the county. To cut the argument short, the results show that the country values computed by the two methods are practically identical. For the State as a whole last year, the aggregate true value by the method of adding assessment districts differed from the aggregate true value based upon the unit method by less than $^1/_{100}$ of one per cent. We investigated forty counties with special care, thirty-six of which have, up to the present time, been calculated according to both methods. A detailed comparison of the results by each method for the thirty-six counties is given below. The aggregate for the thirty-six counties differed by less than one-fourth of one per cent. One county showed a deviation of 18 per cent, and another one of 15 per cent; one showed a deviation of from 5 to 6 per cent; two from 4 to 5 per cent; seven from 2 to 3 per cent; ten from 1 to 2

County Values Secured by Adding the Values of Each Assessment District Compared with County Values Secured by Treating All the sales of Each County as a Unit.

County—	Value by Adding Districts	Value by Unit Method	Error Per Cent
Ashland	9,554,100	10,987,800	15.00
Barron	13,568,845	13,612,934	0.32
Bayfield	12,113,704	11,831,800	2.32
Buffalo	12,358,428	12,140,400	1.76
Chippewa	17,963,086	17,764,500	1.11
Dane	85,367,248	85,499,000	0.14
Dodge	57,114,994	56,547,400	0.99
Douglas	30,809,170	29,276,800	4.97
Eau Claire	16,346,145	16,772,800	2.61
Fond du Lac	52,519,089	52,512,600	0.01
Grant	36,868,674	38,431,400	4.24
Green Lake	15,890,670	15,706,400	1.16
Iowa	24,633,487	24,655,600	0.09
Juneau	12,991,194	13,685,600	5.34
Kenosha	25,578,650	25,228,500	1.37
La Crosse	24,446,479	24,441,000	0.02
Langlade	11,437,105	11,196,600	2.10
Lincoln	9,857,406	9,705,620	1.54
Manitowoc**	35,623,196	34,738,400	2.48

County—	Value by Adding Districts	Value by Unit Method	Error Per Cent
Marathon	29,173,087	29,267,400	0.32
Marinette	16,415,384	16,527,000	0.68
Milwaukee	330,909,372	330,381,000	0.17
Monroe	18,945,261	18,726,200	1.16
Oconto	13,708,242	13,495,500	1.55
Outagamie	38,199.474	38,883,980	1.79
Ozaukee	16,384,072	15,946,028	2.67
Pepin	4.481,402	4,416,200	1.45
Price	7,403,342	7,362,500	0.55
Racine	43,603,952	43,439,800	0.38
St. Croix	18,331,412	18,753,800	2.30
Taylor	8,822,773	8,857,100	0.39
Vernon	18,190,963	18,236,200	0.25
Vilas	7,311,084	5,942,260	18.72
Waukesha	40,343,861	39,499,800	2.09
Waupaca**	18,315,066	18,311,000	0.53
Wood	18,139,757	18,094,800	0.25
Total	1,153,620,174	1,150,825,722	0.24

**The true values for Manitowoc and Waupaca apply to a year earlier than the rest of figures, owing to the fact that the unit estimates for the present year have not been prepared in the case of those two counties.

per cent, and fourteen showed deviations of less than one per cent. In four counties showing a difference of more than 4½ per cent, I may add. a cursory examination of the conditions told us at the very beginning that the sales were not representative. and special care was taken to correct the difficulty, with the result that the discrepancy between the two totals was somewhat increased, as of course it should have been. In only one county, Grant, were we at all surprised by the showing. Taken as a whole, these figures make it plain that misrepresentation or unfair sampling is not a serious problem; and that where it does occur it is usually apparent on the face and can be provided for. The deviations noted above, when compared with the margin of error to which any method of estimating true values is inevitably subject. are in reality negligible. Suppose for instance that a county is placed 10 per cent too low

and that its share of the State tax is $100,000. The result is that it unjustly dumps the munificent sum of $10,000 from its own shoulders, to be divided up and shared by the seventy other counties of the State. Yet an error as high as 10 per cent and a state tax upon any one county as great as $100,000 are very rare in Wisconsin in these days.

In concluding this particular phase of the discussion it may be well to add that our general experience, the net impression resulting from years of continuous work in this field, altogether supports the conclusions above stated. Nothing is commoner than for excited and perfectly sincere partisans to attack the sales method on the ground that a given class of property is assessed at an abnormal proportion of true value. But nineteen times out of twenty when one investigates the charge one finds either that this claim is without foundation or that the particular class of property receives its fair representation in the sales, which makes the peculiarity of assessment meaningless.

By far the weightiest factor in this criticism of the representative character of sales data, is the current belief —would it be too much to call it the "universal belief?"— that large and valuable properties are assessed at an abnormally low proportion of their true value, while they are likely to be under-represented in the sales. The general prevalence of this opinion entitles it to great respect; and has led us. for instance, to make special efforts to obtain data concerning large sales. The record, in many cases shows a consideration of "$1 and other valuable considerations." We have made a practice of asking for the facts in the more important "$1 sales," and find a surprisingly large percentage of the parties willing to give the facts when they understand the use which is to be made of them.

But on the whole, the evidence which we have gathered

upon this subject leads us to believe that in Wisconsin, at least, there is little direct relation between the size or value and the under-assessment of *real property,* and that such relation of this kind as does exist is offset, in its effects upon the true values, by securing what is substantially a fair representation in the sales of the various classes of property. With respect to personal property, the case may be different; in fact we have reason to believe that it is different.

This conclusion might be drawn logically from the fact that in the larger cities as a rule estimates of true values made from all the sales treated as a unit do not differ materially from estimates made by adding the separately computed ward values: and it is in the cities that the most of the large properties and large sales are found. But the conclusion is also supported by rather comprehensive statistics bearing directly on the point. These statistics, based upon 18,315 good sales in nine representative counties and classified so as to show the ratios of assessed to true value for properties of different value, indicate in unmistakable fashion the following facts: (a) That very small parcels, particularly those worth less than $500, are assessed at a distinctly higher ration than other property; (b) that very valuable estates, particularly those worth more than $50,000, are assessed at a noticeably lower ratio than property in general; (c) that between these extremes the assessment is remarkably regular, showing little or no tendency to diminish as the value of the property increases; (d) and that the upper half of the properties ranged according to size (that is to say. "the more valuable" properties correctly defined) are assessed at only a slightly lower ratio than the lower half, or the "less valuable" properties. These results, it should be added, hold good for all the counties considered separately with one exception—a small unimportant county, in which the pressure of tax-

ation is so excessively high that assessors have been forced to take the line of least resistance in increasing the assessment rolls. In this one county, and no other, there is a regular decrease of the proportionate assessment as the value of the property increases.

The quality or completeness of the assessment varies then only in the extreme groups. If these extreme groups receive their proper representation in the sales no harm results from the difference in assessment. The considerations adduced above, and in particular the agreement of the results by the unit and other methods in the cities, establish a strong presumption that the extreme groups are properly represented in the sales, or that if they are misrepresented, their comparative unimportance prevents them from materially distorting the results.

Ratio of Assessed to True Value in Groups Classified by Value of Property.

Nine Wisconsin Counties.

Value of Property	No. of Sales	Assessed Value	Selling Price	Ratio Ass't to True Value Per Cent
Under $500	4,126	$ 692,522	$1,094,730	63.25
500- 999	3,667	1,435,995	2,562,089	56.03
1,000- 1,999	4,807	3,743,091	6,749,091	55.46
2,000- 2,999	2,283	2,907,832	5,369,595	54.13
3,000- 3,999	1,127	2,087,243	3,755,662	55.56
4,000- 4,999	694	1,666,686	2,991,228	55.70
5,000- 7,499	913	2,992,769	5,576,033	53.66
7,500- 9,999	331	1,448,324	2,750,473	52.64
10,000-19,999	293	1,984,794	3,697,319	53.67
20,000-49,999	58	873,400	1,514,645	57.66
50,000 and over	16	830,096	1,764,975	47.03
Total	18,315	20,662,752	37,825,840	54.61
Under $4,000	16,010	10,866,683	19,531,167	55.64
Over $4,000	2,305	9,796,069	18,294,673	53.55

III. DO SALES REVEAL TRUE VALUES?

There are a number of other criticisms aimed at the sales method, the most serious of which, curiously enough, are ultra-theoretical in nature and demand for their final

solution an answer to that metaphysical riddle which has perplexed the philosophers for centuries: what is value? For the substance of these objections is that selling prices do not represent real values.

I shall not try to settle that question here. It will never receive a complete answer until science has plumbed the depths of the ultimate mystery of man. Fortunately, however, after decades of controversy political economy has come to a practically unanimous conclusion concerning a few of the fundamental notions of value which are directly at point in this discussion. It is agreed, for instance, that the value of a thing depends upon its power to satisfy human want; that the character, or quality or moral significance of the want is of no consequence in this immediate connection; and that there is no economic value apart from men's estimates of the want-satisfying power of things. This man wants land to till it, another to build on it, a third to sell it, a fourth to rent it, a fifth because it satisfies a mysterious land hunger, a sixth because land ownership improves the social standing of the owner. In the creation of land values these and a thousand other human desires participate. The desire to improve one's social standing may be, and historically has often been, a more powerful factor in determining land values, than the motive of ordinary business profit. Each desire plays its part, great or small, according as the community attaches to it much or little importance. The essence of value is estimation; why men rank one desire above the other is from our viewpoint immaterial; how much they rank the one above the other is all important. Value *is* valuation.

There is, therefore, no point to the many criticisms of the sales method which assume, sometimes implicitly, sometime explicity, that there is some sort of an intrinsic value more concrete and definite than human estimate. There is no other value to look for. Critics have stood

before the Wisconsin tax commission, for instance, and contended that if land in one of the older southern counties of the State earns $100 a year it should not be taxed on a higher valuation than land earning a similar annual sum in one of the undeveloped northern counties, although the first parcel might sell for more than the second. In reality these critics were contending for an income tax. The simple fact that people are willing to pay more for one parcel of land that yields $100 a year than for another parcel which yields the same amount is a controlling consideration so long as we have a property tax and the law directs assessors to appraise property at "the full value which could ordinarily be obtained therefore at private sale."

But if value is mere valuation, what right have we to exclude from our data sales to municipal corporations, the so-called "sucker sales," and similar abnormal transfers.

The answer is simply that the chance of selling land to the government or a railroad or a "sucker" is not a regular, permanent, commercial opportunity, but distinctly a "gamble," and the price obtained does not represent the value which could *ordinarily* be obtained at private sale. The chance is almost always present in a remote, dim way, and may be supposed to create part, though an exceedingly small part, of the desire which leads men to purchase land. But to include the few cases in which the chance is realized would be like—and I think the illustration clears up the difficulty—giving to each lottery ticket the value of the highest prize. To include a sale to a city or a "sucker sale" is to treat a remote possibility as an average occurrence. Moreover, there are other reasons for their exclusion, the most important of which is the fact that when such abnormal sales are recorded the full price is almost always stated in the deed, while the prices of large numbers of normal sales are concealed. The real estate speculator who catches a "suck-

er" always enters the price in the deed that other potential "suckers" who run may the more easily read. To include abnormal sales of this kind, therefore, would give them an exaggerated representation in the data. Even if they were not otherwise defective such sales should be ruled out on the grounds of over-representation.

Value is nothing more than the estimate of the average man, and the expert's appraisal is nothing more than his estimate of what the general run of purchasers will give. As Mr. W. A. Somers, who has possibly given more study to the valuation of real estate than any other man in this country has aptly said: "To ascertain the value of anything ask one who knows. His answer will be what he thinks it worth based upon his thinking that he knows what others think it worth." If all this is true it follows that the sales method, carefully applied, is not only a good method of ascertaining the true value of real estate, but it may legitimately be singled out as *the* best method of ascertaining such values. For our estimates are never so sure, never so careful, never so conservative as when they are backed by our money. "Put up or shut up!" That vulgar phrase contains in this connection a world of apposite philosophy.

But although sales furnish good evidence, one might almost say conclusive evidence of the value of that part of a stock of goods which is sold, modern economists are always careful to point out that such sales do not necessarily determine the value of the remaining part of the stock. On the contrary they sedulously maintain that the value of the remaining stock is problematical, "potential" to use their ordinary term, so that the major portion of our problem still remain: how to determine the most plausible, the most likely price which the whole mass of goods or property would ordinarily sell for at

private sale. On that point sales data are not necessarily conclusive.

On the fundamental and exceedingly difficult questions presented by this aspect of the problem I am obliged to confess that I have been unable to gather evidence which is conclusive even to my own mind. It is easy to theorize on the subject, but hard to obtain that tangible kind of testimony which the practical importance of the subject demands. However, I hope to keep at work upon the subject, and when in the course of the years the Academy shall again devote its annual session to the subject of taxation I hope to be able to lay before it concrete data which will be of some little service at least in determining the exact way in which a limited number of sales may be employed to appraise the vast aggregate of property whose value in some way they unquestionably represent.

TAXATION OF RAILROAD PROPERTY

By William W. Baldwin

Taxation, as we know it in this country, is not a science; its various forms are mere expediencies. The Englishman who wrote, about three hundred years ago, what was probably the first book upon modern taxation, said: "Those bear it most who least complain." In our time there seems a growing disposition to make those bear it most whose complaints we can best afford to ignore. This, as some one has remarked, is taxation, not according to ability, but according to vulnerability. The old saw that an event is as certain as death and taxes, is not founded upon present-day experience in taxation; taxes are certain upon some persons and some things; they are not certain upon all persons and all things.

The lack of agreement among economists and scholars upon the subject goes without saying. One magnifies the General Property tax as stronger than ever; another denounces it as abominable and obsolete. One approves an Income Tax as ideal and just; another condemns it as partisan, socialistic and the parent of perjury. One demands that moneys and credits be reached for taxation, even if the inquisition and the dooming chamber are invoked; another would repeal all laws requiring the listing of moneys and credits, as entailing more corruption of morals than the revenue to be derived will justify. One holds that a Federal Inheritance Tax law is the correct means of diminishing swollen fortunes; another says that the federal government should never be permitted to compete with the states in seeking sources of revenue. One writer upholds the doctrine of the diffusion of taxes in its most extended application, while an-

other of equally wide repute characterizes it as so very superficial as scarcely to deserve a refutation. One official advocates a scheme for the federal taxation of interstate commerce, which all the other writers oppose as chimerical, because no State will surrender its right to tax the property created within its borders and protected by its laws.

It is little wonder that among the plain people who make the legislatures and are themselves the legislators, knowledge of the subject is limited, and that much of the legislation is crude and unscientific.

CORRECT INFORMATION DIFFICULT TO PROCURE

While investigations and reports and books upon the subject of railroad taxation are plentiful, not only is correct information hard to get, but much that we receive misleads more than it enlightens. For illustration, the Interstate Commerce Commission annually prints a table of taxes paid per mile of railroad track, by States, ranging from $1,470 in Massachusetts to $109 in Texas. Measured by ability, there are railroads in the West and South which pay a much higher tax rate than the more prosperous eastern lines. A leading eastern road, with gross earnings of $39,000 per mile and net earnings $12,000, pays $8 in taxes out of each $100 that it earns above expenses, while the railroads of Iowa with $7,114 gross receipts per mile and $2,231 net receipts, pay, as a whole, $10 in taxes out of each $100 that their property earns.

That government table means little and teaches little. But agitators in Texas and elsewhere use it to show that the people of Massachusetts get twelve times more per mile in taxes from railroads than they receive, as an argument for increasing railroad taxes in their State. But the comparison is not made in Massachusetts as an argument for reducing the tax rate there.

More widely effective, and far more misleading, is the

argument based upon theoretical estimates of the commercial values of railroads, by States, prepared for the report of the census of 1900; among them, Iowa, $35,000 per mile; Nebraska, $45,200, and Minnesota, $59,800. No attempt was or could be made by the Census enumerators to approximate what it would cost to now duplicate the roads. There are very few persons in the country who really know with accuracy upon what these Census estimates were based; but there are many who know that the railroads of Iowa, mile for mile, are worth more than those of Nebraska or Minnesota.

The Census Bureau accepted and announced estimates by States, largely upon theories that were first promulgated in Michigan as an expedient for increasing railroad taxes in that State in response to a violent political agitation. They are described as based upon a capitalization of net earnings at certain rates. These rates were obtained for the census by making computations of the prices of railway securities during the inflated market of the first six months of 1904.

Their estimates, as published, are used freely in arguments for raising taxes in States where they will serve that purpose, and by others to prove that the railroad capitalization of the country is not excessive; but as economic facts they have little value, and their announcement has done much more harm than good. Their usefulness can be somewhat tested as applied to the Burlington railroad.

In making their valuation of that road the census people used four rates for capitalizing its earnings; two applied to what they designated Shareholders' Interests, that is, a rate of 3.86 per cent upon what they called "the divided interest," taking the stock at $181.20 per share, and a rate of 1.59 per cent upon "undivided interests," whatever that may be. Upon what they designated as "Bondholders' Interest" two rates were used, one of 3.91 per cent, based

on "sale prices," and a rate of 4.01 per cent, based on "offers without sales." The composite or resultant of these four rates was a rate of 4.75 per cent for capitalizing net earnings.

No changes in Burlington securities since then would materially change this rate, which if applied to the $20,729,000, earnings of last year, less taxes, would make a valuation of $437,000,000 for the road. That is over $50,000 per mile. The road is now capitalized at $30,000 per mile. But if the stock is taken at their suggested price of $181.20 per share, and the bonds outstanding, less cash and securities in Sinking Funds, are then added, the valuation of the property is $352,267,368. In other words, the valuation of the Burlington road is increased 25 per cent above all figures of inflated stock market quotations simply by this device of capitalizing earnings in very prosperous years at very low rates.

Similar exaggerated results were worked out in the census for all the roads in the country. This paper valuation which was found for the Burlington property was, according to my understanding, distributed to the eleven States in which it is located, upon a track-mile basis, although the average value of a mile of this road in Illinois or Wisconsin is three times the value in Wyoming or Kansas. In many other cases distribution was made on a basis of gross earnings.

Anticipating the use to which these figures would be put as arguments for increasing taxes upon railroads, the Census Bulletin declares that in those States where it is the purpose of the law to appraise railway property at its true cash value, their estimates fairly measure values for the purpose of taxation. This language, it seems to me, should be strongly condemned. In every State where valuations are the basis of taxation it is the avowed purpose to ascertain true cash value, as a matter of course. Better have no census than misleading statistics.

LIMITED BENEFIT FROM COURT DECISIONS

In the search for correct economic principles in taxation, not much aid can be derived from the courts. The courts are not supposed to make the laws; they interpret them.

State revenue is a paramount consideration. Every refinement of argument and construction of language is employed, and perhaps properly, to sustain a tax law. A State tax upon freight passing from one State to another is invalid because it may obstruct interstate commerce, but a tax upon the receipts from carrying the same freight in the same cars, is perfectly good.

It was once illegal to tax the same property twice. Now it is lawful to value a railroad as an entirety and so tax it; then to locally assess its terminals, depots, etc., and subject them to local rates, without diminution of the entire valuation; then to tax against the corporation the capital stock which represents the same property; then to tax the earnings of the same road, and, in addition, levy a State privilege tax, while cities and towns are authorized to require the road to also pay an occupation tax.

The courts sustain double, and, if necessary, quadruple taxation of the same railroad if the methods employed are called franchise taxes, or capital stock taxes—the earnings being designated as a means of ascertaining the value of the franchise, and the other methods being called licenses or excises or charges for the privilege of doing business.

It is a correct rule of law that one State cannot tax property that is located in another State. But the general practice now is to value a railroad as an entirety and, where it is advantageous, to distribute such valuation upon a mileage proportion. Under this practice States without terminal properties import them from other

States and tax them, while States which have them, tax them twice—once in valuing the road as a unit and again by taxing them locally in cities and towns.

WHAT IS A FRANCHISE?

The question of franchises comes up in all tax discussions. Massachusetts describes the tax upon the capital stock of railroads as a tax upon the franchise. Kentucky has created a special board of valuation to assess railroad franchises. Illinois once provided a formula for valuing franchises which has been in practical disuse for thirty years. Nebraska recently about doubled railroad valuations and taxes, and when the authorities were asked why, they replied that they were valuing the franchises. State after State has adopted the same verbiage, and followed the same methods.

What are the taxable franchises of a railroad company —not in strict judicial parlance, but in the economic sense, as elements in a valuation of property? Census Bulletin No. 21 is a detailed scientific description in nearly 100 pages of the methods used for valuing the railroads of the United States. The word "franchise" is scarcely used in the Bulletin. The franchises of a railroad as features or elements of value in an economic sense were not present in the minds of the census experts. Why? Because, economically, and as things whose value can be determined in dollars, they do not exist in property owned by a railroad company any more than in property individually owned. Values to be taxed can be expressed in dollars. He who states that he valued franchises ought to be able to state what franchises he valued and what estimate he placed upon each. Will a consideration of what have been judicially designated as railroad franchises show that this is done?

The Supreme Court of the United States, in the Southern Pacific cases, defined railroad franchise taxes as pay-

ments for the exercise of privileges, and then named three privileges: First, the privilege of existence. Now, that is paid for at the time of organizing; it is nominal in cost, and is substantially the same for all corporations, whether their property is much or little. Second, the privilege of charging toll, that is, of taking pay for services—the natural right of men. If an individual or a partnership is not taxed for the privilege of receiving pay for services why, economically, should the same individuals be taxed for exercising the same privilege or right as a corporation? A law that was intended to exact payment by a corporation for that privilege would manifestly require such payment at the time of organization, and all corporations would pay the same fee or a fee graduated by the tolls. There is no such law. Third, the privilege of exercising the power of eminent domain. That is a power which the State reserves against every land owner in order that it may build a railroad or have one built. Without this reservation no railroad could ever be constructed. It is always exercised during the period of construction, and is worth as much to one corporation as to another. It takes nothing from the land owner to give to the company; full compensation is required before the taking. If this was something to be paid for, as a privilege. the law would fix the rate so that we might know in advance what its exercise would cost. There is no such idea in the law.

Whenever men proceed in a given case to tax railroads upon theories which they defend as a valuation of the corporate franchises, they pay no attention to these Supreme Court definitions.

Prof. H. C. Adams, in a recent address at Buffalo, gave a much wider definition. He said that franchise value is the value of a business in excess of the value of its tangible property, and, secondly, the value of the talent, skill and ability with which it is conducted. As

the skill and ability applied to the property produce the surplus above tangible value, this definition is that franchise value is a term for expressing success, following skill and good fortune in the conduct of an enterprise.

As if to further emphasize a want of appreciation of the Supreme Court's definition of what franchises are, Professor Adams has persuaded the Michigan authorities and others to regard the following features in the business of a railroad as "franchises" to be assessed and taxed. I use his language:

1st. The possession of traffic not exposed to competition—such as local traffic.

2d. The possession of traffic held by established connections.

3d. The benefit of economies made possible by density of traffic.

4th. The value of the organization and vitality of the industries served by a railroad, and the value of the organization and vitality of the railroad itself.

Elaborating still further the definition of railroad franchises that should be taxed, he said: "Intelligence, sobriety and willingness on the part of laborers to submit themselves to discipline are conditions under which industries exist and which make them succeed."

"The railroads of the North are more valuable than those of the South on account of the nature of the employees and the people."

"If the schools of Michigan were disorganized for a generation, the railroads would not be worth very much."

This line of argument seems to completely submerge and obliterate the principle laid down by the Supreme Court in the Southern Pacific case, that railroad franchises are "privileges," and that the valuation of these franchises for taxation is the exacting of a payment for such privileges. There is no logical connection in thought between such grant of privileges by the State to a rail-

road company and its good fortune, for instance, in having located a railroad in the north rather than in the south, or in Michigan, where there are good schools, rather than in a State where there are not such good schools. In other words, it is no longer a question of franchises, but of good fortune or success in location or business. What is taxed is the success and not the franchise.

The Supreme Court itself, in subsequent cases, in order to uphold doubtful tax laws, likewise ignores, if it does not repudiate, the franchise ideas that seemed controlling in the Southern Pacific cases. In the Express Company cases and the Henderson Bridge case, "Unity of use" becomes the paramount element in value and constitutes the main ingredient in the assessment of the intangible property of a corporation.

This view is certainly remote from the idea that specific franchises are privileges, for the use of which, as such, payment is required through taxation. All use of property is use in unity with other property, and it is an ideality to conceive of value as resulting from mere unity of use in the case of corporate property alone. Judge Brewer seems to realize this by saying, in the Express Company case, that the good will of an established industry is the thing of value that must be recognized. It is the good will that is taxed, and not the property nor the franchise.

In forty-one States railroads are taxed upon a valuation, and every excessive valuation is defended as a "valuation of franchises," and there is not in any State nor by any tribunal a definition of what is meant by franchises that differs materially from some one or more of the foregoing definitions. What economic idea do they convey within the meaning of tax laws? The only measure suggested of the value of any of these franchises is income. How indefinite this idea of the taxation of cor-

porate franchise may become, and how demoralizing as an instrument of revenue, is disclosed in the following language of the Southern Pacific decision referred to: "The taxation of a franchise has no limitation; its value is not measured like that of property, but may be ten thousand or ten hundred thousand dollars as the legislature may choose." Then follows, appropriately, the ominous truism of Chief Justice Marshall that, "The power to tax is the power to destroy." Substitute "state board of assessors," or "state tax commission," or "executive council," or "state board of equalization" for the word "Legislature" and the position of railroad property under provisions for the assessment and taxation of corporate franchises is portrayed—its taxation has small likeness to that of other property, is without limit, and practically without rule.

THE ASSESSMENT OF INTANGIBLE VALUES

As suggested, the prevailing method in the taxation of railroads is called a valuation method, or a form of general property tax. One of the expressions most frequently used in connection with the phrase corporate franchises is "intangible value," and assessors often explain increases in taxation by saying that they have been assessing intangible values.

What is intangible value? Will it conduce any to clearness by taking the case of a merchant's stock of goods? Fashion plays an important part in business. A stock of goods up to date and in fashion may make a business profitable, in comparison with an unfashionable stock, which has cost the same. This profit or the ability to make it is intangible value. How shall it be reached for taxation?

Suppose the owners of the prosperous store incorporate. Do we apply the prevailing theories and tax that intangible value? If so, the goods will be valued at

full cash value, say $40,000, and pay the local rates. If the capital stock is $40,000 and pays 10 per cent dividends and has a market value of $200 per share, the capital stock will be valued at $80,000. Deducting the tangible valuation leaves $40,000 for intangible value to be assessed at the state rate, a total valuation of $80,000, while the goods and business of the neighboring firm, who did not incorporate, are assessed at $40,000 and pay local rates only. That method ascertains intangible value from market quotations of capital stock—the Massachusetts method.

The other method is the capitalization of net earnings. If the profits of the prosperous store are $4.000, they will be capitalized at 5 per cent, showing a taxable value of $80,000. Or, an allowance of 4 per cent will be made upon the value of the tangible property—$40,000—that is, $1,600. This is described as an "Annuity deducted for Capital." Being deemed a sure return, this is fixed at 4 per cent. Deducting this from $4,000 of income leaves $2,400, which, being capitalized at 7 per cent, shows intangible value $34,285. which, added to the $40,000 tangible value, gives a taxable valuation of $74,285, compared with the assessment of $40,000 upon the neighboring store. That is the Michigan plan as applied to railroads, and is described in the Michigan formula as "Capitaization of Surplus."

Who can say that this correctly describes the process of taxation of the farming business, or the mercantile business, or that of manufacturing, or of any other class of business in his State except that of railroading?

There is this element of intangible value in every prosperous business. It is represented by income and the income gives value to shares of stock. What property is worth for purposes of income and sale it is worth for purposes of taxation. But in no State is there a pretense of administering the general property tax so as

to reach this surplus or intangible value, unless the owners of the property incorporate; in few States (except Massachusetts) is there a serious pretense of enforcing it against any corporation, except railroad, telegraph, and express companies.

THE VALUATION METHOD OF TAXING RAILROADS

Some form of a property tax based upon a valuation has now been adopted in most of the States. It is easy enough to see how the desire to apply to railroads the general property tax originated. Assuming that property is the best measure of ability, the theory of making a valuation of a railroad and subjecting it to the ordinary tax levies is a plausible theory. How it works in practice can only be understood from knowledge of the methods employed in various States. In many of them different rates are used from those applied to other property.

Connecticut levies ten mills against railroads upon a valuation based upon market quotations of stocks and bonds. The rate upon other bonds was fixed by law a few years ago at two mills, and has since been increased to four. Why should the investment in railway bonds be taxed five times or three times the rate upon other bonds?

The real and personal property in that State, probably does not pay to exceed seven mills upon its actual value.

Massachusetts levies seventeen mills upon railroads, which is perhaps double the rate actually paid by other property of the State as a whole, at full value.

Where a class of property is undeniably assessed at full value, under a general property tax, its owners should not be required to pay higher rates than are paid by the owners of other property. The extent to which lands and lots are undervalued and personal property is both

concealed and undervalued is notorious. Writers have called attention to the instance of the city of Brooklyn, where, in a comparatively recent year, personal property paid only one and a quarter per cent of the whole tax. Professor Seligman, commenting upon this and other cases, says:

"These striking figures become ridiculous when it is remembered that the value of personal property far exceeds that of real estate in such communities."

In the 1907 report of the Massachusetts Joint Committee upon taxation they say: "The amount of personal property taxes actually paid varies from 2 to 10 per cent."

Seven-eighths of the personal property in these States is owned by the persons who own the real estate.

When the plan for a valuation of railroad property, plus a valuation of the franchise or intangible elements based upon a capitalization of earnings, came into operation in Michigan in 1902, it was recognized by all fair-minded persons that a tax rate which was derived from considering only half the general property, if applied to railroads, would make it a class rate and would double the tax burden upon that class of property owners very unjustly. To correct this, the legislature of Michigan, in 1905, passed what is known as the Galbraith law. This law made it the duty of the tax commission to ascertain and determine the true cash value of all property in Michigan, for the purpose of fixing the average rate to apply to railroads. The passage of the act aroused a storm of protest, and it was promptly nullified by the Supreme Court.

The report of the tax commissioners of that State for 1906 says:

"The Census Bureau has just issued a Bulletin showing the wealth of Michigan, in 1904, exclusive of railroads, to be $3,000,000,000, consisting of $2,019,000 000 real estate and $987,000,000 personal."

They were compelled by law to find their rate applicable to railroads (17.4 mills) from a valuation of only $1,574,000,000, one-half the true value of the general property.

A similar condition exists in Wisconsin, although not to the same degree. The owners of Wisconsin railroads pay a tax rate of about 11 mills, while those who own the other property pay, probably, 7 mills. In Iowa, the average rate upon the full value of all property in the State is about 7 mills; in Missouri it is less.

The methods of valuation are various, and are, of course, as important as the rate. Questions of the cost of a railroad, or what it can be reproduced for, are only taken as the starting point in valuations for taxation where they are considered at all. In States where advanced theories on the subject are said to prevail, such as Massachusetts, Connecticut and New York, they are entirely ignored.

In Massachusetts, one-half the railroad taxes are derived from levies upon real estate, assessed at full cash value, as land, by local assessors, and paying local rates. The capital stock is then valued at market quotations on May 1. From this valuation is deducted the real estate assessment and upon the remainder there is levied a tax rate of about 16.87 mills. The bonds are subject to local assessment, but, whenever possible, the owners rightfully conceal them from taxation. The capital stock assessment is called a valuation of the corporate franchise.

In Connecticut, there is no real estate valuation and no consideration given to any question except the market value of the stocks and bonds. Upon this valuation of securities is levied a state rate of 10 mills.

In New York four-fifths of the taxes paid by railroads are realized from assessments by each local assessor of the entire road in his district. There are no limitations upon the assessor as to his exercise of judgment. He

must consider the use, which includes earnings, franchises and intangible values. There is also levied a tax of 1½ mills upon each dollar in value of the capital stock —such value to be fixed or reviewed by the state comptroller. The capital stock may or may not mean the shares; it may mean the property investment; the valuation may be made from market quotations or by capitalizing earnings, or from dividends or by any other rule the comptroller may select. In addition there is levied in New York a state tax of 5 mills upon the gross receipts of every railroad in the State.

OBJECTIONS TO MARKET QUOTATIONS

The extent to which value is determined from market quotations of securities and the inaccuracy of the method have long been recognized.

The value of a railroad may be much more or much less than as indicated by market quotations. Northern Pacific stock sold at $11 per share and at $1,000, both within a comparatively short period. When quoted at 11 the road was worth much more than the quotation indicated; when quoted at 1.000 it was worth much less. Conditions in Massachusetts and Connecticut may make market quotations more nearly an approximation to value than elsewhere—the traffic is more stable, the securities can be used in the reserves of banks and insurance companies and so forth. But the principle is not sound as applied to Western and Southern roads. Many roads have been in bankruptcy in recent years, including such prominent systems as the Santa Fe, Union Pacific, Wabash, Frisco, Northern Pacific, Baltimore & Ohio and Reading. Others may become bankrupt at any time. When that time comes, no assessing board will accept the market quotations of their stock as the measure of the value of the property.

All these stocks are under speculative influences; much

capital stock is the product of reorganizations, forced or speculative, and represents large sums of wasted and unprofitable capital which, nevertheless, has a quotable market value. Besides, there are serious practical difficulties of distribution. Every system has its main lines and branches, extending into several States. The road is not taxable as a whole, but by States and by counties. Its capital stock is one. Distribution of its value in proportion to mileage might be reasonable if there was main line only, but is not a decent approximation when applied to branches. States having main line chiefly, ignore mileage proportion of the capital stock valuation, while States with branches chiefly, insist upon it, and the courts uphold them both. A Michigan official, in condemning this method, said that out of seventy-five railroads which they were called upon to appraise there were only seven respecting which the information was adequate to make an appraisal on the basis of market quotations.

The stocks and bonds of a railroad represent everything the company owns, whether used in operating the road or not. Many of them own extensive lands, and mining, and steamship and other interests, and the stocks and bonds of other corporations, and much of this outside property is separately taxed. The value of all this separate property is reflected in the market quotations of the stock. The ownership by the Great Northern company of ore lands carried the market quotations of its stock up to 348, but those lands were not a part of its railway and the value of the railroad could not be determined from such market quotations.

THE MICHIGAN PLAN

In 1901 Michigan abandoned a tax upon gross receipts and adopted what they designate as a general property tax system for railroads, based on a valuation upon which is levied a State rate. The report of the

state board for 1902 describes the plans as follows: By a certain process of calculation they determined the net earnings of each road. An appraisal of the value of each line was made by Professor Cooley, upon which valuation was computed an annuity of 4 per cent, with 1 per cent allowance for taxes. The sum of these being deducted from net earnings, the balance was called surplus—corporate surplus. This surplus was capitalized at various rates for different roads of 4 to 10 per cent. and the result called "franchise value," or "intangible value," to which was added the appraised value, and the sum of these constituted the valuation of the property upon which the rate of 17.4 mills was levied.

It is understood that the present state board, or some of them, do not approve this method, but they retain the valuations which it produced for them.

Part of the criticism they make is that this is virtually an income tax upon the business, but that no other business in the State pays an income tax. The author of the plan, being asked the difference between this plan and an income tax, said: "I don't think there is any difference except the formal difference that in one case the tax is levied upon a valuation discovered from the earnings. and in the other case it is levied directly upon the earnings."

THE RATES OF CAPITALIZATION

It is apparent that the entire efficiency of this method depends upon sufficiently low rates for capitalization. A valuation can, of course, be doubled by the simple expedient of capitalizing income at 4 instead of 8 per cent. In view of the history of railroad income in the past twenty years, the influences of competition, the control of rates by legislatures and commissions, the strength of labor unions, the dependence upon good crops and good times and all the known vicissitudes of the business, a rate of 10 per cent for capitalizing railroad income is

not unreasonable. The Michigan board fixed 3½ per cent for the Michigan Central.

Professor Emory Johnson, by taking a reasonable rate for capitalization, computed $3,227,000 as the franchise value of that road, which Professor H. C. Adams had fixed at $18,259,880. The board adopted the larger valuation. That was politics.

Professor Adams defends these low rates for capitalizing income upon socialistic grounds, claiming that the so-called "surplus" of a railroad is a socially produced value; that the State is a joint owner therein, and is merely taking its own through taxation. This view involves, of course, a radical change in the whole system.

It will no longer be the assessment of property in proportion to value for the expense of government. It will be the seizure by the State of what the chosen expert may advise to be the proper share of the State in a socially produced value.

That is not taxation; it is appropriation.

THESE THEORIES APPLY TO ALL STATES

No discussion of this question can proceed very far which does not take into account the development of these theories. They have already changed the tax systems of Michigan and Wisconsin. They have doubled the taxes upon railroad property in Indiana and Nebraska, and largely increased them in Kentucky and other States. State after State has adopted laws making the property of railroads the nominal basis for their taxation, with a constant tendency to make income the real basis, by providing that the valuation shall include franchises and intangible elements and then making income the measure of franchise and intangible values.

In Nebraska and Indiana it is practically impossible to ascertain the real basis. The valuation is doubled, and inquiry elicits the reply that corporate franchises

are being assessed, and perhaps information may escape that market values of stocks and bonds have been considered, or that the earnings have been capitalized at some rate. So administered, this system may, under political influences, become an arbitrary, uncertain, unequal and secret dooming-chamber system. It has the excesses but not the openness of the Massachusetts and Connecticut methods. It has been characterized as playing the game of taxation with loaded dice.

SOME EXAMPLES OF RAILROAD TAXES

How much it will be carried to an extreme remains to be seen. When these methods were installed in Michigan, in 1901, the railroads of that State were paying 14 per cent of their net income in taxes. During the five years it has now been in operation they have paid in taxes each year an average of 32 per cent of their earnings. The taxes of the Michigan Central were increased from $420,000 to $850,000 annually, and of the North-Western from $87,000 to $220,000.

The Michigan Central was, prior to 1902, paying 4 per cent of its gross receipts for taxes, and 15 per cent of its net; it is now paying 28 per cent of its net. In the past five years the entire net receipts of the North-Western in Michigan were $674,000; the taxes paid were $1,096,000. The owners of that property, for the privilege of serving the people of Michigan with good transportation facilities, paid out in taxes $400,000 more than they received. This was not idle property but a well-managed business in five very prosperous years.

The net earnings of all Massachusetts railroads last year were $6,502 per mile and the taxes $1,513, or 23 per cent. The Boston & Albany earned $10,604 per mile and paid $3,576 in taxes, or 33 per cent.

There has just been printed a report of the joint special committee on taxation, consisting of fifteen mem-

bers of the Massachusetts legislature, appointed in 1906, which is therefore the last word upon the subject of taxation of railroad franchises in that State. Among other recommendations, they say: "It seems clear to us that in levying the corporate franchise tax, the bonds at their fair cash value should be included with the capital stock at its fair cash value."

The result is described by them in these words: "This proposed change would increase the taxes of the railroad corporations alone about 50 per cent. Such an increase in taxes would cause real embarrassment, and in the case of some of the gas companies and street railway companies we fear virtual bankruptcy." This means that the State, in protecting industries with government, is devouring them.

This increase, when made, will result in taking from Massachusetts railroads, as a whole, in taxes, $34 out of every $100 they can earn in good times, and from the Boston & Albany $49 out of every $100. In bad times the proportion will be larger.

Who would dare propose a tax of 15 per cent upon the net income of all industrial enterprises in Massachusetts? How long would Massachusetts keep its industries if they were subjected to such a tax?

Upon information received from circulars addressed to the officials of every county in Iowa, it has been repeatedly stated in public, without contradiction, that the average tax paid in that State upon farm lands which produce $4 per acre net cash as rental, does not exceed 25 cents per acre—a net earnings tax of 6 per cent. This is upon the farm, not upon the farmer. The farmer who owns the land also owns the personal property. This includes notes, bank deposits and other intangibles. These are seldom listed for taxation. The only item of personalty owned by the farmer which appears upon the assessment roll is certain live stock at extremely low

valuations, with liberal exemptions. The farming industry in the West does not pay, in taxes, 6 per cent of its net earnings, and in Massachusetts probably not 10 per cent.

THE GENERAL PROPERTY TAX

I have referred to some of the more important methods coming into use for applying the general property tax to railroads. How the system itself, as a tax system, is regarded by scholars and social economists, is forcibly stated by Professor Seligman, who says:

"The general property tax as actually administered is beyond all doubt one of the worst taxes known in the civilized world. Because of its attempt to tax intangible as well as tangible things, it sins against the cardinal rules of uniformity, of equality and of universality of taxation. It puts a premium on dishonesty and debauches the public conscience; it reduces deception to a system, and makes a science of knavery; it presses hardest on those least able to pay; it imposes double taxation on one man and grants entire immunity to the next. In short, the general property tax is so flagrantly inequitable, that its retention can be explained only through ignorance or inertia. It is the cause of such crying injustice that its alteration or its abolition must become the battle cry of every statesman and reformer."

There is no business or industry to which these anathemas of the general property tax can more properly be directed, if present tendencies continue, than that conducted by railway companies. The valuation system is made to sin against uniformity and equality, and puts premiums on dishonesty under the guise of franchise taxes and levies upon intangible values.

In what way can reform be realized? Not in modifications or ameliorations of the general property tax. All these varied and nominal forms of valuation and

of assessing corporate franchises and intangible elements are, in truth, income taxes; they are levies upon the wealth that is represented by income. Mr. Justice Miller. in that forcible opinion in the State Railroad Tax cases, so often quoted from, said: "An assessment of the visible property of the road may not include all its wealth."—"A company is so rich that after paying expenses and interest it declares large dividends. * * * Here is another element of wealth." While described in form as a franchise tax, the substance, as an economic proposition, is a tax upon wealth measured by income.

WHAT IS A BETTER SYSTEM?

Reform lies in the direction of abandonment of these methods for the taxation of business enterprises. Every other civilized nation in the world has abandoned them.

The vast and growing wealth of the country, not in things that can be seen, is measured by income and can be reached through income. There is no honesty in treating the owners of railroads as a class by themselves, nor the profit that is made in conducting the business of transportation as a socially produced value which the State may appropriate or confiscate through taxation, any more than in treating the profits of a merchant or a factory as socially produced and jointly owned by the public.

This wealth cannot be fairly assessed for taxation through a percentage of gross receipts. Taxes paid by a railroad are contributions of the owners and are supposed to be in proportion to ability, as indicated by wealth evidenced by the income which the owners receive. From 50 to 90 per cent of the receipts of railroads are not such income; they are not paid to the owners; they are paid to employes in wages and for other expenses. Taxes upon such receipts are not taxes upon income, but upon outgo—not upon wealth, but

upon the labor fund. If that fund is only sufficient to meet the expense of operation then a tax upon receipts becomes a tax upon labor and not upon property.

If property and labor on a railroad together receive $8,000 per mile, and labor earns and receives $6,000 of this and property $2,000, taxes should be levied upon the $2,000 at a rate comparable with rates paid by other property, which manifestly is never done where gross receipts are taxed, because the levy is made upon what both the labor and the property receive.

In the two States of Maine and Minnesota, which retain the gross earnings tax, it is not possible to form an opinion upon the fundamental question of all taxation—equality between taxpayers, that is, whether the owners of railroads are being taxed in proportion to ability, more or less than other property owners. There is no standard, because no other class of persons or property is taxed upon a proportion of gross receipts, and as to most property and business it is wholly impracticable.

Taxation of gross receipts results in the most flagrant inequality as between different properties. There are railroads in Minnesota which pay out practically all their income in wages and expenses of operation, and others perhaps pay only one-half. The owners of some roads, therefore, pay twice or three times as much in proportion to ability or wealth as others. The less the real ability to pay, the greater, relatively, may be their taxation.

One of the most serious objections to the present system of taxation of gross receipts is its political character. It is fixed by the legislature, and for reasons already suggested, there is no standard and every determination must, therefore, necessarily be only a rude guess, influenced largely by politics. The natural impulse is to please constituents by relieving them from taxation, especially if it can be done at the expense of non-residents and non-voters.

Writers of the highest character, seeing the abuses into which we are drifting, advocate a tax upon net receipts, in lieu of all other taxes. This would be a tax upon the property and upon the wealth which the property annually produces. Being direct upon income, it would be an honest tax compared with the indirectness of taxing income through the device of a valuation of property by capitalizing income. It would have the merit of simplicity, compared with the present obscurity. Under suitable provisions, there would be no double taxation, and the earnings on property in one State would not be taxed in another State.

If the railroads could manufacture accounts and manipulate their expenses so as to shift the amount of net income between States, that would bar the adoption of a tax upon net earnings. But this would be impossible under strict and correct rules for accounting which the States would necessarily adopt. No one questions that the State of Iowa now gets a correct statement of net earnings. Any State could claim a share of the entire net earnings of the road not less than its proportion upon the basis of car mileage, or upon a gross receipts proportion, or some basis universally admitted to be fair. Once public attention is concentrated upon the subject, the proper ascertainment of net earnings by States need not be a difficult problem.

The difficult and important problem would be the rate. This ought to be determined free from politics or political intrigue. The operation of a railroad is the conducting of a complicated business enterprise far more than it is the mere ownership of property. The rate of tax should be as nearly as possible the same proportion of its income that other property and business enterprises in the State are being taxed—to be ascertained by a thorough and disinterested investigation of such a

character as to command the entire confidence of the people.

Is such an investigation practicable?

The rate would not necessarily be fixed at 6 per cent because the farming business pays in taxes, on the average, 6 per cent of its net receipts, nor at 5 per cent because the merchandising business pays out in taxes 5 per cent of its earnings, nor at 4 per cent because that is the rate of the manufacturer.

But unless the railroad business is to be placed in a class by itself, why shall its income be taxed at 15 per cent, or 30 per cent, while the other industries of the State are only taxed 6 per cent of their income? Should the State not find out whether such excessive taxes are bein levied, and how can this be ascertained better than by adopting a net earnings basis with suitable checks and limitations to ensure equality and uniformity in its operation? That might result in exempting from taxation a railroad that cannot pay operating expenses, but would there be any demand for the taxation of such a public service, gratuitously performed? If such a demand should arise, some feature of the property tax could be applied in such cases, but the exceptions would be so insignificant as not to change the rule.

A railroad is as much an instrumentality of commerce as a ship. No government in the world that has any shipping, except the United States, taxes ships as property. Some of them tax the net earnings at very low rates, because they do not wish to impair their commercial facilities.

A writer of great ability said, in a pamphlet issued last week: "When it is considered that railroads in this country are controlled and regulated as public highways, the levying of taxes upon them is an anomalous proceeding." We are not frightened by government anomalies. We are surrounded by them.

The suggestion that excessive taxation will impair commercial facilities and deter the investment of private capital in railroads falls, at this time, upon deaf ears. The people seem to welcome every plausible argument that makes the profits of the railroad business a socially produced value belonging to the State, which may therefore be appropriated through taxation, and likewise every legislative rate reduction that tends to bring these profits down to the minimum. That persistence in such policies, however plausible the legal theories upon which they are based, will bring to an end the investment of private capital in railroads, needs not the tongue of prophecy.

TAXATION OF RAILROAD PROPERTY

(Continued)

By CLARENCE B. MILLER

The presentation of the subject of railroad taxation by Mr. Baldwin is an unusually strong exposition of the position the railroads themselves take in respect to it. Undoubtedly the railroads consider themselves the objects of attack and bitter hostility on the part of the public. There are two reasons why the railroads so consider the situation. First, such is the appearance when a comparison is made between the attitude of the people some decades ago, and that witnessed today. Second, the attitude of the people as expressed in recent legislation displays an intrinsic distrust, as well as an emphatic desire to curb and control. The taxation of railroads is merely one element of the railroad problem, but the whole problem is up for attention, and taxation is receiving attention together with the other elements.

Should one seek the cause of the changed attitude on the part of the people toward railroads his task would be simple. It is merely disappointment over that which the railroads have returned to the public in consideration for the vast power, blind trust and great wealth they have hitherto received from the public.

At the outset the public looked upon a railroad as a great boon, and as the most important means to its welfare. To secure a railroad has been the earliest ambition of each area of newly-settled territory throughout the United States. To get a railroad the people of a new territory have been willing to barter away almost their

birthright. Their zeal in this regard had much reason to support it, for the history of modern empire building is almost synonymous with railroad building. The prosperity of any section bears a striking relation to its transportation facilities. The value of an article often depends entirely upon getting it to a distant market. To encourage and assist in railroad building the people gave up great quantities of treasure and some most important privileges. Thus, they gave to railroads the power of eminent domain—that power through the exercise of which a railroad can take private property whenever and wherever that property is coveted without regard to whether the owner consents or not. They gave to each railroad the exclusive right to certain carrying business, as each railroad enjoys non-competitive business in certain territory. They gave to many of the large railroads immense land grants, whose value was often beyond the first cost of the construction of the roads. The people have generally given to an incoming railroad free right of way. Many counties. villages and cities have given bonuses, either cash or in bonds, to railroads, and in such large amounts as to cripple them financially for decades. It has also been common for municipalities to make large subscriptions to the capital stock of incoming railroads. It was formerly the custom either to exempt railroads from taxation or to make their taxes much lighter than that borne by other classes of property. The people have thus surrendered up to railroads power, privileges and wealth with amazing prodigality. The reason for this conduct is to be found in the expected public benefit to be derived from the railroads. The people and the railroads should supplement each other, their fortunes should be bound up together, prosperity for one should mean prosperity for the other. In fact the prosperity of any community is largely dependent upon the way its railroads discharge their duty to the public.

By reason of these contributions which the railroads have received from the public, and by reason of the public service in which they are engaged, they owe a large and ever extending duty to the public, and the public in its governmental capacity has a right to regulate to a certain degree the operation and conduct of the railroads. Notwithstanding this duty resting upon the railroads to operate their systems for the welfare of the public, reserving to themselves reasonable returns upon their investment, we find that railroads have recently been forgetting all interests save their own, and have been vastly transcending their corporate powers. Many localities have been dwarfed and their interests sacrificed to the building up artificially of distant centers and distant regions. Rate discriminations have been made in favor of large and powerful concerns giving them such an advantage that they have been able to destroy the business of the man of small means. The consolidation of railroads on an enormous scale has placed in the hands of a few individuals, a power greater than that in centuries past ever yielded by emperors or kings. The people may well look with alarm when a few hold within their grasp the economic destinies of empires. The power and wealth thus centralized have been used for purposes wholly foreign to transportation—such as the building and operating of elevators, buying and selling town sites, coal mines, iron mines and other mineral deposits. Then, too, politics have been controlled and the policies of a State moulded by railroad power. Realizing that this industrial institution they have created and endowed with life and power is inclined to run riot, the people have determined to cease feeding it and to curb and control it to a certain extent.

It is natural that attention should early be turned to the matter of taxation. Most railroads in their earlier days have enjoyed a peculiar exemption from tax con-

tributions. Many of the charters freed the railroads from taxation for a term of years, others placed a lower tax on them than was paid by other classes of property. In many state constitutions, as for example, that of Minnesota, can be found provisions tending to make difficult any increase in railroad taxation. We have gradually been working away from this tax favoritism attitude, and each year new laws are designed to place upon railroads a larger and more just share of the tax burden. No two States are taking equal steps, no two are making the journey by traveling the same route. Furthermore, progress has been very slow. It can be generally said that railroad property is not paying taxes equally with other classes of property. Mr. Baldwin thinks railroads are being required to pay too much in taxes, but I believe that he has in mind a comparison rather with the days when railroads enjoyed partial exemptions. than with other classes of property today. He cites the case of the C. & N. W. Ry. in northern Michigan. There must be some mistake about this, for that portion of the system is engaged in carrying iron ore, and all the world knows how very profitable that is. The criticism of the Michigan system is perhaps just in respect to its application to certain weak and unimportant lines, but this is the fault of application not of principle. I firmly believe Michigan has taken an important step in advance in recognizing certain elements of taxable value hitherto ignored in railroads. Competent experts make a valuation of the physical properties of a railway system, consisting of roadbed, tracks, cars, locomotives, depots, terminals and the like. Then the gross earnings of the system are capitalized at 3½ per cent—which is perhaps too low—and the sum is generally far greater than the physical valuation. The difference between the two represents the earning power of non-physical elements. These non-physical elements consist of the following:

1. Franchise right to do a railroad business and to carry on the public service.

2. The natural monopoly which a railroad has of certain local business, and all business not open to competition.

3. The established connections a road has made with other railroads—they acting as feeders.

4. The density of the population in the territory of a railroad.

5. The vigor and prosperity of the industries in the country through which it runs, and the effectiveness of its own organization.

To the above might be added one more,—the absence of heavy grades, ravines to be bridged and the like. An inspection of these elements, which the Michigan system uses as a basis to tax that part of the earning power of a railroad not represented by its physical plant, reveals that with the possible exception of the third, all the non-physical elements are contributed by the country or people, and there is especial reason why the people should receive back from them something in the way of taxes.

The public can exercise control over the profits to be earned by railroads in two ways: (1) By reducing rates, and (2) by increasing the taxes. It may be said that railroads should not be taxed because the people have to pay it. But this is true of every article of producing property. Again, the best of supervision cannot control rates with exactness. and a contribution in the way of taxes is a certain and stable method of securing a return to the people. The tax rate must not be such as to make carrying rates unreasonably high in order that a fair return may be had to the stockholders on their investment, but railroad property should pay taxes equally with other forms of property.

Several States, notably Wisconsin and Michigan, are now working to secure an ad valorem tax on the actual

value of the railroad property, and yet a great majority of the States still cling to some form of the gross earnings tax. This is attractive because it is easily collected. Minnesota, in company with Maine and Maryland, has a straight gross earnings tax. In Minnesota these taxes are all paid to the State, the local sub-divisions not receiving any part of the same. In Minnesota this tax is also in lieu of all other taxes and there results to the local sub-divisions an ever-increasing hardship,—in that it exempts railroad property from paying local assessments. The improvement of the cities and villages in Minnesota is being seriously handicapped by this item. Railroads have gradually acquired valuable terminals inside the cities and other municipalities until a large percentage of the most valuable property is withdrawn from the local tax rolls. These railroad properties abutt on streets and other places where public improvements are a necessity, and yet these improvements are entirely prevented or long delayed by the inability to place a part of the burden upon the railroad property. This same difficulty is found in those regions where drainage is desired. Large areas of swamp lands are traversed by railroads or are bordered by railroad property, and unless this property can be made to bear a part of the burden, drainage must be greatly hindered.

Until within four years the gross earnings tax in Minnesota has been 3 per cent. It is now 4 per cent. This is a much lower rate than is paid by other classes of property in this State. The average farm pays more than this. In cities property pays from 8 to 20 per cent of its gross earnings, and all this property pays local assessments in addition. The gross earnings tax might easily be raised to 5 per cent, and, in addition, railroads be required to pay local assessments. But if only one of the two should be added, let it be the local assessments.

It is probable that the time will again come when the railroads and the people will mutually understand and admire each other, but not until the railroads have become the servants of the people, devoted to the interests of the public welfare. An honest and fairly generous attitude by the railroads regarding taxation, giving accurate data in respect to the amount of investment, value of the properties. net and gross income, would enable the public to deal more quickly and intelligently with this element of the problem, and aid very materially in re-establishing confidence and good will.

Third Session

TAXATION OF PERSONAL PROPERTY

THE TAXATION OF CREDITS AND MONEY

By Nils P. Haugen

In most of the States credits are taxable like other personal property, with the difference that the creditor may deduct his indebtedness from his credits and be assessed for the remainder only. This is in harmony with the recognized principle of equitable taxation, that each individual shall contribute towards the support of government according to his ability. I, therefore, assume this to be the sense in which the term credit taxation is used here, and shall so treat it.

In New York, and in Minnesota the action of the last session of your legislature, credits secured by real estate mortgage are placed in a separate class and made exempt. a recording fee being charged in lieu of taxes. By your law, a fee of 50 cents on each $100 of indebtedness secured by the mortgage is charged when the mortgage is filed for record. It is called a tax; but it violates every principle of taxation. It bears no relation to the general tax rate or to the public need of revenue. It violates the rule of uniformity, as the rate on a mortgage due in one year is ten times that of one due in ten years. The mortgage of the small and modest borrower who is unable to get the longer credit, bears necessarily the higher burden. The ten thousand dollar mortgage will have a decided advantage in the tax rate over the

hundred dollar mortgage. It brings in revenue by the old and direct hold-up method, and may serve to delude the public to assent to the exemption of the creditor. As a source of revenue it should be reserved for emergencies, like the federal stamp tax during the Spanish-American War. Those of us who have had to do with conveyancing know that the mortgagor almost always pays the recording fee, and while the internal revenue stamp was required, he paid it also. He is very sure to pay this tax.

The advocates of credit exemption have, as a rule, been silent as to money. Evidently they think that the owner of money is able so to hide it that he can evade the law. Their silence on the subject of money is a tacit endorsement of the evasion of legal and moral duty by the tax payer. Money brings the owner no income when unemployed. Converted into a credit, it does. If credits are to be exempted, money certainly should be, for of the two it is of least value to the owner. They should be treated alike as they are in the subject as submitted for this discussion.

In Massachusetts and Wisconsin the mortgagee's interest is made an interest in the land mortgaged, and made taxable as such in the assessment district where the land is located. But as mortgages provide that the mortgagor shall pay all taxes and assessments upon the mortgaged premises, the result in both States has been that the mortgagee's interest is exempt as to him. The mortgagor pays all taxes upon the premises, and there is nothing left to assess against the mortgagee.

OBJECTIONS TO CREDIT TAXATION

The principal objections raised to the taxation of credits are:

First. That credits are not property;

Second. That a tax on credits is necessarily shifted

by the creditor to the debtor in an advanced rate of interest;

Third. That the law to tax credits is impossible of enforcement.

I. ARE CREDITS PROPERTY?

Courts have been almost unanimous in holding that credits are property for purposes of taxation; but it is sometimes claimed that "economically" they should not be so considered. This was the position taken by my colleagues on the Wisconsin tax commission in the report of 1903. After the publication of that report the supreme court of Wisconsin in Kingsley vs. Merrill, 122 Wis. 185, where the issue was squarely before it, held "credits" to be property. But the strongest expression by any court on the subject is found in Adams Express Company vs. Ohio, 166 U. S. 219, where Justice Brewer speaking for the supreme court of the United States uses the following vigorous language:

"B.,a solvent man, purchases from A. certain property, and gives A. his promise to pay, say, $100,000 therefore. Such promise may or may not be evidenced by a note or other written instrument. The property conveyed to B. may or may not be of the value of $100,000. If there be nothing in the way of fraud or misrepresentation to invalidate that transaction, there exists a legal promise on the part of B. to pay A. $100,000. That promise is a part of A.'s property. It is something of value, something on which he will receive cash, and which he can sell in the markets of the community for cash. It is as certainly property, and property of value, as if it were a building or a steamboat, and it is as justly subject to taxation. It matters not in what this intangible property consists—whether privileges, corporate franchises, contracts, or obligations. It is enough that it is property which though intangible exists, which has

value, produces income and passes current in the markets of the world. To ignore this intangible property, or to hold that it is not subject to taxation, at its accepted value, is to eliminate from the reach of the taxing power a large portion of the wealth of the country."

As a matter of law therefore the question must be considered settled.

It is the law in Wisconsin, and I believe in most of the States, that the balance only of credits above indebtedness is liable to taxation. This is certainly in harmony with the general rule of measuring tax liability by ability to pay and avoids the interminable creation of taxable credits of which Mr. David A. Wells in his work on Taxation makes a bugaboo. The endless chain of credits cannot create taxable property interminably by the reloaning of the same amount by the debtor to a new debtor as supposed by Mr. Wells under the system of taxing credits as we know it, for each credit after the first would be offset by an equal amount of indebtedness leaving nothing to be taxed.

Not only are credits property, but its owners are generally of a class as to whose ability to pay there is no question. Credits, more than any other form of property, are a distinct index of wealth.

The advocates of credit exemption cite the fact that European countries do not tax credits directly, as an argument in favor of their exemption, but they ignore the fact that those countries operate under an entirely different system of taxation, having quite generally abandoned the general property tax as we know it and substituted for it an income tax. So far from releasing the creditor from his duties of citizenship, not one of them exempts the income from credits and many impose a higher rate upon incomes from investments than they do upon professional incomes or wages. They have

substituted under their system the creditor for the credit, and they certainly do not favor the creditor class.

Some of our courts have gone beyond the strictly legal features of the question and have discussed it in the light of good economics. Chief Justice Doe, of New Hampshire, took occasion to express himself as follows:

"By a selection of subjects for taxation, or other methods of classifying persons, requiring some to pay their neighbors' share, the community would be divided into inferiors and superiors, and the agency established for the common benefit of all would be carried on, without authority, for the private interest or the emolument of the privileged class, to whom for no public purpose, others would be forced to pay annual tribute." This he likens to a system of slavery vesting "in one class the entire product of the industry of the other." 60 N. H., 255.

And Judge Payne, of the supreme court of Wisconsin, in an early case said:

"The small property owners who constitute the great mass of the people usually pay their taxes without question, and seldom combine for the purpose of procuring any special privileges or exemptions. But capital, always keen-eyed and vigilant, always equally ready to grasp at the profit and shrink from the burden—often able to bring to bear powerful and dangerous combinations of influence upon legislative bodies—will be sure to take advantage of such a construction, and to shift upon others the burdens which itself ought to bear." Kneeland vs. Milwaukee, 15 Wis. 507.

And the Ohio supreme court said:

"The goods and wares of the merchant require his unremitting care and labor to make them profitable; a farm with all its implements and stock would be wholly unproductive without the necessary toil of the agriculturist; and the materials, machinery, etc., of the mechanic

and manufacturer are made productive only by their being accompanied with the labor of the operatives. A tax upon all those classes of property which derive their productiveness from labor is, to some extent, a tax upon labor. But a tax upon credits is a tax upon capital alone, in its most productive form, unmingled with labor. To exempt credits from taxation, and throw the whole burden upon those forms of property which derive their productiveness from labor, would afford a most unfair and unjust advantage to capital over labor, oppressive in its consequences to the productive interests of the country." Exchange Bank vs. Hines, 3 Ohio State 26.

There is but a short step from the contention that credits are not property to the further claim that franchises and all other rights and privileges of an intangible character are not property. The public conscience would rebel at this date against the exemption from any share in the public burdens of the very properties which are the basis of our largest individual fortunes. It is also the kind of property which oftener than any other needs and seeks the protection of the courts and thus increases the tax which it tries to avoid.

II. The Shifting of the Tax.

Books have been written on this subject, but the doctors disagree, varying from those who advocate the absolute theory of shifting of Adam Smith to those who say that the tendency of taxes is to remain where laid. There is very little satisfaction in studying the literature upon the subject. It remains pure theory with little, if any, positive evidence upon which deductions are based. I have tried to go through Wagner's treatment of incidence in his Finanzwissenchaft, but neither he nor Professor Seligman of Columbia University seems to arrive at any conclusion after discussing the various theories advanced by the writers. Dr. Seligman makes sweeping denunciation of the personal property tax, stating that it is

"no exaggeration to say that the general property tax in the United States is a dismal failure." It is also quite noticeable that in reviewing in the Political Science Quarterly, December 1904, the report of the Wisconsin tax-commission for 1903, Dr. Seligman does not even mention the chapter recommending the exemption of credits. He says the report is noteworthy for its chapter on a state budget, but is ominiously silent as to the chapter on credits. He must have dissented from its reasoning. It took the extreme view that something more than the tax is added to the rate of interest charged upon taxable credits, while in his Incidence of Taxation on page 262 Seligman says, "As between" lender and borrower "a uniform tax on all capital must fall on the lender, that is on the capitalist."

The average tax payer must derive the amount of the tax from some source. The question is whether in the case of credits the amount of the tax is shifted to the borrower in a higher rate of interest, or comes out of the profits of the lender, or is divided between the two. A rather remarkable contribution to the discussion of this question is an article by Prof. Plehn of the California University published in the Yale Review, May, 1899. Prof. Plehn takes the extreme view that the interest rate is increased by the amount of the tax. and evidently thinks he proves his case by the result of the California plan to tax the mortgagee. I believe him mistaken, not only as to the facts he states, but as to the deductions made from his own statistics. Prof. Plehn says: "In any attempt to tax all property, mortgages present a difficulty." Certainly far less difficulty than other credits. Of all ordinary credits they are the most valuable and the most easily found. Prof. Plehn's article seems to proceed upon the theory, that if the tax were equal on all classes of commercial paper, or if all credits were exempt from taxation, they would all draw the same rate

of interest. Let us see if this is true. We will take an example from San Francisco.

The report of 1903 of the commissioner of insurance of California shows that in 1902 the Pacific Mutual Life Insurance company, located at San Francisco, had $1,001,361.53 invested in mortgages, on which it earned $42,698.21, or 4.264 per cent interest. It had $2,008,409.99 invested in stocks and bonds on which it earned $79,576.32, or 3.962 per cent interest. Why did it not sell off its stocks and bonds and invest its funds in mortgages as long as the latter brought it so much greater returns?

California undertook to localize credits secured by mortgage by making the interest of the mortgagee an interest in the land, assessable where the land is located, and made void any contract by which the mortgagor agreed to assume the tax upon the mortgage. By that very act the free competition of outside capital in mortgage loans was necessarily shut out, thus interfering with the operation of the natural economic laws—those principles and forces which underlie, and if untrammeled, regulate and control industry and commerce, including the rate of interest, and which are of infinitely greater potency and force and more unerring in operation than any mere act of the legislature.

In California no outside competition was permitted without subjecting itself to the local regulation. We would naturally expect such a law to increase the rate of interest. Prof. Plehn says that mortgage loans in San Francisco earned on an average, from 1880 to 1898 inclusive, 6.81 per cent interest, while first-class commercial paper, left free to competition, earned 4.73 per cent.

The constitutional amendment relating to the taxation of mortgages was adopted in California in 1879. For the six months ending April 1, 1880, the rates of interest earned by San Francisco banks on real estate loans

"taxed" are given at 8.91, and on bonds and first-class commercial paper "untaxed" at 4.32 per cent.

In 1898 we find that the rate on the "taxed" securities had fallen to 7.19 per cent. and on "untaxed" it had increased to 4.90 per cent.

The supreme court of California had held in 1876 that credits were not property under their constitution. Agitation resulting in the new constitution followed.

The first six months under the new constitution covers securities, nearly all of which must have been executed prior to the time when the new constitution took effect. Still we find a decline from 8.91 per cent to 8.78 per cent in the rate of interest on securities falling within its provisions. According to the reasoning of Dr. Plehn interest should have advanced at this time.

The rate on "untaxed" securities likewise shows a decline. Other influences were evidently at work.

Loans on bonds and on first-class commercial paper, "untaxed," as stated by Dr. Plehn, must include long time municipal and perhaps state and national bonds, and the best long time railroad bonds, in large blocks, which always and under all circumstances are preferred by sound financial institutions and favored with a very low rate of interest.

Real estate mortgages represent relatively small sums for short periods.

I deem it a fair conclusion to say that with the abnormal conditions created by the Calfornia attempt to lay an iron hand on the mortgagee, nothing of value can be deduced by the statistics submitted by Dr. Plehn, even if they truly represented the situation. He says he obtained his statistical information from three banks as to the rates of interest, and the 11th United States Census as to the real estate for the years 1880 to 1889 inclusive. He does not go behind the returns. He says, "The average difference for 19 years between the rate of

interest on mortgages and the rate on other loans equally secure but untaxed, was 2.73 per cent. This, then, is the amount by which the tax raises the rate of interest."

He gives no force to the fact that mortgage loans are in small amounts, not readily convertible, that taxes and other matters affecting the security must be watched, and that most of the mortgages being in San Francisco fire risk and care of insurance must have influenced the interest rate.

He has entirely overlooked the fact that to evade the law the interest rate has, in how many instances it is impossible to ascertain, been misstated in the records on which he relies.

The supreme court of California in Hewitt vs. Dean, 91 Cal., 60, had before it a note secured by mortgage which provided for interest to be compounded, if not paid, at 12½ per cent. The statement of facts proceeds: "At the same time with the execution of the note and mortgage, and as a part of the same transaction, the plaintiffs executed to the defendants the following instrument: 'For valuable consideration I hereby promise and agree to give credit for 2½ per cent of the 12½ per cent interest on the mortgage note signed Mrs. Cornelia R. Dean and G. L. Dean in my favor, dated October 29, 1887, provided said Deans shall******present to me proper official receipts showing the payment of all taxes against the property' " mortgaged.

The court held this to be a voluntary offer made by the mortgagee, which was in no wise binding or enforceable against the mortgagors, and was not a contract in contravention of the constitution.

Had the parties taken advantage of the offer made them the rate of interest paid would have been 2½ per cent less than that which appeared of record and probably entered into Mr. Plehn's calculations. How many such mortgages he did include neither he nor

anyone else can say, but it proves the absolute unreliability of his statistics. I refer to his article because I deem his statistics worthless and misleading. Even taking them as given they do not bear out his theory.

I would expect the California law to affect the rate of interest and am surprised that an examination of the insurance commissioner's tables fails to prove it. In 1871 the rate on real estate loans was 12 per cent, and that rate steadily declined from that time on, disregarding minor fluctuations. There was no interruption in the falling of the rate of interest caused by the new constitution taking effect or by the agitation accompanying its adoption. The tables fail entirely to substantiate the charge that the rate of increased interest in California was shifted to the borrower. There was no increase.

The principal objection to the California law must be found in the fact that it shut out all competitive capital from outside the State and thus excluded those economic forces which always affect and regulate prices of commodities. including the use of money. But even there the statistics fail to show that the debtor was any worse off than before. The rate of interest on the "taxed" has fallen more than on the "untaxed" paper. I think we are all agreed that unless the debtor will receive some measure of benefit from the exemption of credits, the argument of shifting fails.

But we have the experience of other States and notably Massachusetts and Wisconsin.

MASSACHUSETTS.

In Massachusetts the interest of the mortgagee is declared to be an interest in the land, and the mortgagor may agree to pay the tax on the mortgagee's interest. The tax commission of that State, in its report of 1897, says: "The practical effect is that all mortgages stipulate for the payment of the tax by the mort-

gagor or borrower. The mortgagee is not directly affected by the tax and may be said to be virtually exempt." Here, then, certainly is a case that ought to determine whether the borrower gets the benefit of a lower rate of interest if his creditor is exempt.

The law was adopted in 1881, before which time both the mortgage and the land were taxable to their respective owners.

On page 38 of the report referred to, the Massachusetts commission says that "in loans on farming real estate the rate of interest has failed to decline." There is a tone of disappointment in this admission. The money lender has disappointed his friends who believed that if exempt he would divide with his debtor the tax donated to him by the public. Mortgages on real estate outside of Massachusetts are taxable to their holders the same as other personal property.

The report of the majority does not enter very extensively into a discussion of the Massachusetts law on the subject of mortgages and presents no statistics, but a minority report by Commissioner George Edwin McNeill throws much light on the subject, both by its thorough discussion of the general principles involved and by the valuable statistics with which he supplements and illustrates his points. He agrees with the majority that mortgages on Massachusetts real estate are exempt from taxation by virtue of their law. He produces tables of statistics confirming his conclusions that exempting mortgage credits has resulted in no benefit to the debtor; that, on the contrary, it has been a direct injury to him in imposing on him a higher rate without lowering the rate of interest and that the only party benefited is the creditor.

The law exempting mortgages took effect in 1881. The tables printed with the report show that the average rates of interest on mortgage securities in Massachusetts

were in 1880, 6.122 per cent, and in 1889, 5.312 per cent, showing a decline of .81 or about four-fifths of 1 per cent during the period covering the time when the act exempting mortgages took effect. This is not as great a reduction as that of other securities not affected by the law referred to. Take for the same period five first-class securities not affected by that law, and the rate of interest realized upon them declined much more than interest on the mortgage securities which were exempted as the following shows:

	Rates or Int. Realizable					Decline from 1880 to 1889
	1880	1882	1883	1886	1889	Inc.
Boston & Albany's 7's of 1892	4.600	3.790	4.000	3.350	3.650	.950
U. S. 4's after 1907	3.630	2.870	2.870	2.440	2.120	1.510
Mass. 5's of 1894	3.940	3.315	3.250	2.710	2.780	1.160
Maine 6's	4.190	3.440	3.250		3.000	1.190
New Hampshire 6's	4.460	3.830	3.500	3.370	3.110	1.350

A comparison of the tables shows that the rate on mortgages fell less than on any one of the other securities. The average rate on these securities was, in 1880, 4.24 per cent, and in 1889, 2.932 per cent, a decline of 1.308 per cent, while the rate of interest on mortgages declined only .81 of 1 per cent.

The rates of interest on the investments of savings banks in Massachusetts, mainly in mortgages, which seems to have been taxable under the general law, declined 1.579 per cent in the six years before their mortgages were exempted, and only .377 per cent in the seven years following their exemption. The rates of interest in Maine, Connecticut and Rhode Island are compared with those in Massachusetts, and show that the rate of interest on mortgages actually fell more in Rhode Island from 1880 to 1882, when the decline due to this exemption in Massachusetts must have occurred, without any such change of law to bring it down, than in

Massachusetts. The decline in mortgage rates under the law in Massachusetts, has not been greater than in other states under similar conditions without any such change of law. (p. 221, Mass. Tax Com., 1897.)

Mr. McNeill says: "The increase in the general tax rate caused by the mortgage exemption, and the accompanying savings bank tax reduction, rendered necessary by it, as estimated by Mr. Winn, with approval of the legislative committee of 1883, was $1.06 per thousand of valuation. The legislative committee of 1884 estimated it at $1.64 per thousand. This the borrower had to pay as an additional tax, not only on that part of his land represented by the mortgage, but on his equity above the mortgage as well.********It seems entirely plain, therefore, that the mortgage exemption cured no double taxation, because the lender suffered none, but involved an actual loss to the borrower, increasing thereby the so-called double tax, to say nothing of the losses to the community at large."

The Massachusetts law has had direct evil results on their general system of taxation, in other respects, as the exemption of a class always breeds dissatisfaction and encourages evasion of taxes by others, not so fortunately situated as to be able to avail themselves of the legal exemption.

In his "Incidence of Taxation," on page 187, Dr. Seligman says: "In almost all the writings on Incidence (shifting of taxes), the particular tax under discussion is assumed to be special or exclusive. For purposes of pure theory, this assumption is legitimate, nay, even necessary; for it is only through isolation that we can get a clear picture of the working of a single force******* Other things being equal the more general the tax, the narrower the taxless field to which the persons concerned can migrate; the less general the tax, the greater the chance that the tax will be shifted."

In other words, the exemption of credits would, according to Prof. Seligman, make capitalists convert their property into such forms of credit as would bring them within the exempted area.

WISCONSIN.

It is fair to say that the experience of Wisconsin throws more light upon this question than anything else available. The tax commission in 1903 recommended to the legislature the exemption of all credits. This recommendation was not followed, but the legislature that year passed an act of the same general character as the Massachusetts law which I have discussed. It concerned mortgages only, and in effect exempted them from taxation, and assessors and taxing officials have been so advised and have acted accordingly. Mortgages have paid no tax in Wisconsin since 1902. Other credits remain taxable as formerly. After the report of 1903 and the act exempting mortgages the tax commission caused to be made a thorough and exhaustive examination of the rate of interest of mortgages and other credits. The investigation was under the direct supervision of Dr. Thomas Adams, associate professor of political economy in our State University. The result is published as Appendix B to the report of the Wisconsin tax commission, 1907.

The investigation covered all mortgages recorded for three years prior to the passage of the law, and also for a period of three years after its passage. Between these two three year periods a third period of six months covering the time of agitation while the legislation was pending is treated separately.

The mortgages are also classified with reference to amounts and place of residence of lender.

In Wisconsin, as in other States, the law had not been well enforced and credits had quite generally escaped

the assessor. This was one of the reasons for the creation of the tax commission. The legislature had in 1901 created the office of county supervisor of assessment to have more direct supervision and control of local assessments. These officials entered upon their duties in 1902 and made quite successful efforts that year to add credits to the assessment rolls. The amount of moneys and credits placed on the tax roll that year exceeded that of the preceding year by about $50,000,000. In one agricultural county alone (Grant) where the supervisor was especially active, $4,000,000 of property of this class was placed upon the rolls. I contended in 1903, and have not changed my views, that the recommendation in the report of that year to abandon the taxation of credits was a mistake, especially at the very time when the effort to reach them seemed to be fairly successful.

What has been the result of the exemption of mortgages upon the rate of interest? The investigation shows that the average rate of interest paid upon mortgages since they were exempted from taxation does not vary materially from that which was paid during the three year period preceding their exemption. In fact the rate for the later period is a trifle higher than for the former; 77 per cent of all mortgages in the State represent loans made in the immediate neighborhood. They are transactions between neighbors. Parties making them are not professional money lenders. The man with a little capital to spare prefers to loan it to his neighbor and is more watchful of the security than intent upon a high rate of interest. This is so whether he is taxed or not. As distance separates the lender from the borrower the interest rate increases, except in the case of very large mortgages of $10,000 or more, where the interest is lower. But there are not enough such large mortgages materially to affect the result.

Since the passage of the act of 1903 many mortgages

have inserted in them a proviso that in case mortgages again become taxable as personal property the mortgagor shall pay the tax upon the mortgage as well as the tax upon the real estate mortgaged. A separate classification was made of such mortgages and it was found that the average rate of interest charged in them was higher than the average of similar mortgages without the clause.

The investigation was directed into another channel. We compared the interest rate on mortgages in four border counties with that in adjoining counties in other States. Thus in LaFayette county, Wisconsin, was compared with Jo Daviess county, Illinois. In Illinois mortgages and other credits are taxable. The law is not very well enforced, however, but La Fayette county shows no advantage from the fact that mortgages there are exempt. The vigorous assessment of 1902 and the agitation preceding the passage of the new mortgage law in May, 1903, are noticeable in La Fayette. There was a decided falling off in the number and amount of mortgages contracted in the last half of 1902. The interest rate rose for mortgages of all sizes, the proportion of money borrowed within the district and within the county fell, while the amount borrowed outside the State rose from less than 13 to nearly 35 per cent. The rise in the general average interest rate was only 0.09 of one per cent and appears smaller than it would have been had mortgages not increased rapidly in size. The same average size of mortgages during the middle period of agitation as of the preceding period shows an increase of 0.14 per cent, but even this is only a small fraction of the tax rate which is supposed by the advocates of the shifting theory to be added to the rate of interest.

Comparing the Wisconsin with the Illinois county, we find that Jo Daviess shows up more favorably with respect to interest rates than La Fayette throughout the entire period. La Fayette county gained nothing by the

exemption. Its interest rate was 0.14 per cent higher. both in the first and last epochs; the average rate being 0.07 per cent higher for both counties in the last than in the first period. La Fayette has, however. gained in the increased number of neighborhood loans, while the Illinois county has lost. Under these circumstances we might look for a larger increase in the interest rate in the Illinois county, but other influences have been at work and prosperous years show a falling off in loans. The same general conditions prevail, however, in both these counties.

The two adjoining counties of Marinette, Wisconsin, and Menominee, Mich., were compared. In Michigan a systematic attempt was at the time under discussion made to tax mortgages and accurate statistics of mortgage assessments were at hand. They were and are taxable to the owner in the district wherein he resides. The tax commission of Michigan aided materially in the assessment of mortgages by furnishing each assessing officer a transcript of the record of mortgages owned in his district from the office of each register of deeds in the State. The tax commission was also furnished with information of change of residence of the mortgagee, which it imparted to the assessor of the district to which he had removed. It also had a record of partial payments, and offsets are noted. Likewise assignments.

Comparing the two counties, it appears that in the year 1902, the only year in which a serious attempt was made to reach credits in Wisconsin, the assessment of moneys and credits in Marinette county was increased ten-fold over the previous year. The effect of this was apparent.

In the first half of 1902 an unusually large number of mortgages was recorded. Our assessment is made as of May 1. In the last half of 1902 and first half of 1903 an unusually small number. In Menominee there was no

such decrease. Interest rates, also, show the same influence, reaching the maximum for the whole period of six and one half years in the first half of 1903 in Marinette, while in Menominee they were lower in the last half than in the first half of 1902, and still lower in first half of 1903. Since the exemption of mortgages in Wisconsin Marinette county makes the more favorable showing in practically every way. Interest rates are lower than in Menominee and seem to be falling in Marinette while rising in Menominee. More than 90 per cent of the Marinette mortgages are from Wisconsin lenders, while only fifty per cent of Menominee mortgages are from Michigan lenders. This, however, is no doubt largely due to the fact that Menominee county in the upper peninsula is naturally through railway facilities and otherwise tributary to Wisconsin rather than to Michigan. It is also true that in Marinette about 60 per cent of mortgages in recent years contain an agreement whereby the mortgagor binds himself to pay the tax upon the credit as well as upon the land if the credit shall become taxable as such. The fact that these Michigan mortgages held in Wisconsin are taxable in Wisconsin, our exemption applying only to mortgages upon Wisconsin lands, might be expected to drive the Michigan borrower elsewhere, and that this is not the effect must mean either that the contracts are not insisted upon or that our laws are not enforced. The average tax rate in Marinette in 1904 on the assessed valuation was 2.4233 per cent. The weighted average interest rate during the last period when mortgages were taxable in Michigan and exempt in Wisconsin was 6.64 per cent in Menominee and 6.19 in Marinette, a difference of 0.45 or less than ½ of one per cent on all mortgages. Even this is only a small fraction, about 1-5 of the tax rate. I am unable to give the tax rate in Menominee. In giving the above average interest rate the large mortgages over $2,500 each out-

weigh those of smaller amount. Taking the smaller mortgages, those more typical of the average tax payer and we have the following average weighted interest rates for the same period.

	Marinette County Per cent.	Menominee County Per cent.	Difference Per cent.
Mortgages under $200.....	6.98	6.82	0.16

in favor of Michigan, while in mortgages from $500 to $999 the rate in Wisconsin was 6.26 per cent, and in Michigan 6.73 per cent. or 0.47 per cent in favor of Wisconsin.

This is the strongest case I find in favor of the theory of shifting, but it falls far short of proving that the interest rate is increased by the amount of the tax.

Washington county, Minnesota, and St. Croix county, Wisconsin, were compared, and for this same period when mortgages were taxable, though it would seem not very generally taxed, in Minnesota and exempt in Wisconsin, we find the average weighted interest rate in Wisconsin to have been 6.14 per cent and in Minnesota 5.92 per cent, and in mortgages under $200 7.21 in Wisconsin and 6.56 in Minnesota. In all classes of mortgages the rate was higher in Wisconsin than in Minnesota.

I do not consider Washington a typical Minnesota county. It lies too close to St. Paul and has in it the city of Stillwater. This is also true of Menominee and Marinette counties. Neither is typical of its State.

They are new and undeveloped, each with one quite large city in it.

The most significant comparison made was that of Grant county, Wisconsin, and Clayton county, Iowa, adjoining. Here we have two counties of similar general characteristics in soil. population and economic conditions. Both are thrifty agricultural communities and typical counties of their respective States. In Grant

county in 1902, the year of strenuous assessments, under the guidance of a supervisor who hewed to the line, over four million dollars of moneys and credits were assessed. The same year a little over three million dollars was assessed in Clayton, and a trifle less has been assessed each year since. 1906 falls very little below 1902, and is higher than either 1904 or 1905. The large assessments of moneys and credits in the Iowa county are undoubtedly due to the so-called "tax ferret" system employed. Clayton county has availed itself of this law, and moneys and credits seem to be as fully assessed as other personal property. Dr. Adams says: "While estimates********must always be uncertain, there seems to be no reasonable doubt of the fact that the great majority, if not practically all of the mortgages in Clayton county are actually assessed and taxed."

I insert here the weighted average interest rate for the entire time and for each period covered by the investigation.

WEIGHTED AVERAGE INTEREST RATE.

Grant County, Wis.

Size of Mortgages	Jan. '00 to June '06 Per cent	Jan '00 to Dec. '02 Per cent	Jan. '03 to June '03 Per cent	July '03 to June '06 Per cent
All amounts	5.80	5.61	6.15	5.87
Under $200	6.73	6.44	7.23	6.99
$500 to $999.....	6.19	6.03	6.32	6.30
$2,500 to $4,999.....	5.77	5.56	6.08	5.87

Clayton County, Iowa.

Size of Mortgages	Jan. '00 to June '06 Per cent	Jan '00 to Dec. '02 Per cent	Jan. '03 to June '03 Per cent	July '03 to June '06 Per cent
All amounts	5.69	5.57	5.75	5.81
Under $200	6.92	6.78	7.37	7.05
$500 to $999.....	6.10	5.96	5.88	6.33
$2,500 to $4,999.....	5.63	5.52	5.55	5.76

The total amount of moneys and credits placed upon the assessment roll in Grant County was in

1900	$ 357,996
1901	1,410,600
1902	4,192,668
1903	1,094,806
1904	865,179
1905	711,290
1906	733,420

In Clayton county since 1901 the amount assessed each year has been about three million dollars. There is considerable similarity in the movement of the interest rate in the two counties in spite of the fact that mortgages have been exempt in Wisconsin since June, 1903, while in Iowa, and especially in Clayton county, they have been taxed. The number of mortgages fell off in Clayton as well as in Grant in 1902, but in Grant the number has increased since that year, while it has fallen steadily in Clayton since 1901. The showing seems the more favorable on the whole in Clayton. Interest rates are on the average lower in Clayton. and the increase in interest rates has been less there than in Grant. As to the smaller mortgages the interest rates are a trifle higher in Clayton. What is most surprising is that more money is borrowed within the state in Clayton than in Grant. This is contrary to the common belief that the taxation of credits will drive money out of the state. Finally the number of mortgages in which the mortgagor undertakes to pay the tax on the mortgage, if it is made taxable as personal property, is increasing in Grant and not increasing in Clayton. On the other hand the relative amount of money borrowed outside the state is diminishing in Grant and increasing in Clayton. The average tax rate in Clayton is about three-fourths of one per cent of full and more on assessed value. This is certainly large enough to make the interest in Clayton considerably higher than in Grant on the theory of shifting.

I am not aware that any investigation has been pursued anywhere as thoroughly and impartially and under

as favorable conditions for comparison as that conducted by Dr. Adams for the Wisconsin tax commission. The refutation of the contention that the entire tax is shifted to the borrower seems well established. That some part is shifted under some circumstances seems reasonable, but as far as this investigation shows it is at the best—or worst—only a small fraction of the tax.

The investigation discloses that mortgages in Wisconsin command a slightly higher average rate of interest since they have been exempt than before, while commercial loans made by banks show the reverse of this, their interest rates being slightly lower during the last than the first period. It is true that before the passage of the act of 1903 resulting in exemption of mortgages the law was not well enforced as to the assessment of credits including mortgages. It is also true that during the latter part of the period considered the general money market may have tightened somewhat as to interest rates. That, however, should have manifested itself in commercial loans as well as mortgages.

The theory of shifting put forth by Prof. Plehn and by a majority of the tax commission of Wisconsin in its report of 1903 is certainly not borne out by the investigation made by the commission in 1906.

The advocates of credit exemption generally underestimate the desire of the small capitalist to invest close at hand and the influence he has upon the interest rate.

III Can the Taxation of Moneys and Credits be Successfully Enforced?

None of our laws for the local assessment of property, especially personal property, is enforced even with approximate thoroughness. The local assessors in Wisconsin, and they are probably as conscientious and intelligent as those of other States, in 1905, fell short of the number of horses found by the Tax Commission 65,615;

in the number of neat cattle 241,981. The showing was no better with respect to other tangible personal property. Assessments will never be perfect.

Moneys and credits certainly present additional difficulties. In all matters of assessment and taxation the personal equation can never be eliminated from the administration. Recklessness and extravagance, if not downright dishonesty, of public officials, necessarily result in excessive taxation. Careless assessments result in unequal burdens. No matter what the law may be it cannot supply ability and honesty where those qualities are wanting. Whether we tax credits or not we need better local administration. The burden of the tax is the local tax and it falls relatively heaviest upon the person with but little property and that in sight. His burden is increased by the exemption of credits. Under the activity of the tax commission of Michigan referred to there seems to have been a fair measure of success to reach credits. So successful was this work on the part of the Michigan tax commission that, according to the second report of the commission, of the mortgages recorded in the State and subject to taxation there only a little over 4.5 per cent escaped because of the inability of the officials to locate the owners. This was for the year 1902, but may be considered fairly normal. This compares favorably with the assessment of other personal property in a State like Wisconsin. In Iowa, under the tax ferret system, millions are added to the tax roll annually, very materially reducing the tax rate. In Wisconsin the last average tax rate for the State based on local assessments was 1.61 per cent, while on the full cash value required by law and as found by the tax commission in its state assessment it was 1.07 per cent, or less than 2-3 the rate actually paid by the individual because of the failure of assessors to comply with the law. What is required is a higher regard of official duty by

local officers. This seems to quite an extent to be effected by the direct reading into the local assessments and raising the local rolls by the Michigan tax commission. The Minnesota commission possesses, I believe the same power. The Wisconsin commission does not. This is perhaps a less crude method and one that better recommends itself to the sense of fairness of the tax payers themselves, than does the hiring of tax ferrets under the Iowa law. It would seem more in accordance with true principles of government to leave the collection of taxes, like other public duties, to public officials rather than to turn it over on a percentage basis to outsiders who are more interested in the emoluments coming to themselves than in an impartial administration of the laws. Still the Iowa system has, in the opinion of Gov. Cummins, upon the whole worked well. He says, however, that there is a wide difference of opinion with regard to the law.

It seems a fair conclusion that moneys and credits are more difficult to reach than most other classes of property, but that they can be assessed with proper vigilance to an extent that falls but little below other personal property, and that mortgages can be assessed fully as well as other personal property.

The effort made in Wisconsin in 1902 was fairly successful in counties having good supervision. In counties where the supervisor did not exert himself there was but little betterment of previous methods. But the same holds true as to other personal property. Local assessments in Wisconsin in 1902 of all property, including moneys and credits, was increased 26 per cent over the previous year. Moneys and credits alone were increased 105 per cent or four times the general rate of increase. It is a strange anomaly in legislation that in states like Massachusetts and Wisconsin the law still pursues moneys and unsecured credits, while it exempts mortgages,

the most valuable class and the class that can with reasonable vigilance be reached.

The Tax Rate

One objection raised to the taxation of credits and money is that they are assessed, if at all, at their face, or full value, while other property is generally underassessed. There is force in this objection. The average assessor is not likely to discriminate between two notes of like amount and against equally solvent debtors, one drawing 8 and the other 4 per cent. Still there would be a different value of the two which any bank would recognize if they were presented for discount. But this is a mistake of judgment as to value and is exactly like placing the same value upon two horses, one of which may in fact be worth twice the other, and would be so valued by an expert.

It is true that taking 15 or 20 per cent of the interest on a mortgage for taxes seems high, but investigation shows that returns from other income is about as high.

The tax commission of Wisconsin last year gathered some statistics of cash rentals of rural and urban property in that State, which are presented in its last report. For purposes of accuracy we confined our investigation to cash rentals. In brief the returns of city and village property show that in one of the 35 counties reporting over 30 per cent of the *gross rentals* was paid for taxes; above 20 per cent in four counties, and less than 10 per cent in only one county.

For the 35 counties the average of taxes to *gross* rentals is 17.64 per cent.

Perhaps the most interesting comparison is that which shows what per cent of the income is paid for taxes after insurance and repairs are deducted. The highest rate on this basis exceeds 50 per cent in one county; 20 per cent in 17 counties, and in 9 of the remaining counties

it exceeds 15 per cent. This leaves only 9 counties below 15 per cent and no county is below 10 per cent. The average of tax to net rental is 23.16 per cent.

In our returns of farm property we did not get accurate information of the amount spent for insurance and repairs, hence net incomes could not be computed.

The highest percentage of taxes to gross rentals on farm property is over 50 per cent in one of the northern counties. It exceeds 25 per cent in 5 counties. The average of taxes to gross rentals for the 43 counties reporting is 13.39 per cent, and it is safe to say that the average of taxes to *net* rentals would approach 20 per cent,—probably be between 17 per cent and 20 per cent.

The average rate of interest received upon mortgages in 1904 in Wisconsin was 5.85 per cent. The average rate of taxation as fixed by the tax commission that year was 1.144 per cent, which would make the tax rate 19.55 per cent of the interest received had mortgages remained taxable. The average tax rate would, however, have been lower on all property than that given but for the law resulting in the exemption of mortgages.

The percentage of gross and net income paid for taxes by the eight leading railroads of the State during the last three years has been as follows:

	Of gross Per cent.	Of net Per cent.
1904	5	15.68
1905	5 1-3	15.83
1906	5 1-5	16.10

This is the average of the group of roads.

The result of these investigations, therefore, tends to show that in Wisconsin landlords of city and village property pay about 23 per cent of their net income for taxes; landlords of farm property somewhere between 17 and 20 per cent; the leading railroads of the State

about 16 per cent, and owners of mortgages, if mortgages had remained taxable as they were before 1903 would have paid for taxes on an average about 19½ per cent of the interest received. The interest may in a general sense, I believe, be fairly taken as their net income. Credits then would not pay as high a rate of taxes measured by net income as the city and village property, about the same as farm property, and somewhat more than railroad property.

The interest rate varies materially in different parts of the state. As a rule a low rate of interest and a low tax rate are found in the older and wealthier counties, while both rise as we enter the northern, less developed counties. The tax rate is also relatively high in counties having large cities. In purely agricultural counties relatively low.

The question whether credits shall or shall not be taxed is one that concverns all taxpayers and not merely the creditor class or the debtor class. The average taxpayer belongs to neither of these classes. His interest is to have every individual taxpayer in the district contribute, as he is made to contribute, according to his ability, whether that ability be measured by income or by property. This is not only his interest; it is his absolute right. Let me suppose a case:

A, B and C are the only taxable inhabitants of a town, where it is necessary to raise $600 in taxes. A's property consists in two notes of $5,000 each against B and C drawing 6 per cent interest and assessed at $10,000; B owns a farm assessed at $10,000; C owns a farm assessed at $10,000; a total of $30,000. The rate of taxation would be 2 per cent. A would pay tax on his credits, $200; B would pay tax on his farm, $200; C would pay tax on his farm, $200; total, $600.

Exempt the note, and in order that B and C, the debtors, shall have the benefit of the exemption, A must

reduce the rate of interest from 6 per cent to 4 per cent; and in order that they shall be better off than before he must reduce it below 4 per cent. Paying 4 per cent with credit exemption would leave them just where they were before.

Or suppose B owes for the full value of his land, $10,000, to A, then the assessment and tax would stand thus: A. notes against B, $10,000; B, land, $10,000; C, land, $10,000; a total of $30,000. $600 tax equals 2 per cent of assessment. A, pays $200, B, pays $200, C, pays $200; total of $600. Exempt A's notes and B pays $300 and C pays $300, a total of $600.

B, to be benefited must have more than 1 per cent reduction in interest. One per cent would leave him just where he was before. C would lose $100 in any event. C is an innocent bystander, and still he is mulcted $100 in order that A may be exempt. He has no interest whatever in the private relations of A and B. The property tax as we have it makes the relation of tax to income more striking in the case of credits than in the case of other property, but as I have endeavored to show, the difference is not so great as generally supposed. I am inclined, however, to the opinion that an income tax ought to be substituted for the personal property tax. This would remove the apparent discrimination against creditors.

The administration, however, would have to be changed from the present township system with us, under which assessments of personal property of every kind have proved a dismal failure. The administrative features of any taxation system are all important. However plausible and just the laws, gross injustice will result unless they are impartially and fearlessly enforced.

This would undoubtedly be true under an income tax as well as under a general property tax. Our taxing machinery is very expensive. We assess all property—

or are supposed to—every year. Real estate might be assessed once in five, or perhaps three years, saving the large outlay to 1,500 assessors four years out of five, or two years out of three. The income tax might be administered from the county by a county official under the supervision of the tax commission, and subject to review by it. I believe this would improve our administration and be more equitable than the present system. Then exempt personal property from taxation.

We have in Wisconsin an amendment to the constitution to be voted upon at the next general election authorizing the adoption of an income tax which may be graduated. While I have tried to refute some of the objections raised by the creditor class to the taxation of credits and the absolutely untenable theories advanced to sustain them, the general property tax needs more radical changes to make it just and equal than the mere restoration of credits to the tax roll. The creditor should pay his share. With fairly liberal exemption of small incomes perhaps graduated by the number of dependents in the family much of the injustice now perpetrated under the guise of taxation would be removed. The ubiquitous "poor widow" has been thrust into this discussion. The "poor widow" with a thousand dollar mortgage on which she is compelled to pay taxes is certainly as well able to pay as the more numerous "poor widow" without any mortgage but with one cow not worth one-fortieth as much as the mortgage. No advocate presents her case in tearful tones. No one has asked, in Wisconsin at least, that her property be exempted. If the argument of the creditor class must rest upon this kind of sentiment, why not exempt the property of all widows and get from behind their skirts? Our law takes no notice of the economic condition of the taxpayer. Probably is should. But if so, it must go further than merely to exempt the poor creditor. It would

at least be fair and just to exempt the poor debtor also.

The owners of credits should not be relieved of the first duties of citizenship, for the reason that such a course makes them a favored class, is entirely undemocratic in letter and in spirit, is unjust and wrong in principle, and offers a plausible justification for evasion of taxes by others who with much reason feel that they are unjustly discriminted against. It does not benefit the debtor, the only party who has the right to ask legislative interference, but adds to his taxes a part of the tax that the creditor justly and equitably owes.

THE TAXATION OF MONEY AND CREDITS

By Carl L. Wallace

Taxation is the taking or appropriating such portion of the product or property of a country or community as is necessary for the support of its government, by methods that are not in the nature of extortions, punishments, or confiscations; and with a minimum of cost and trouble to society and its individual taxpayers or contributors.

Or again, a tax is that certain portion of the product of a country which must be devoted to the support of the government.

The cardinal principles of taxation are:

1st. Equality

2nd. Definiteness

3rd. Convenience as to time of payment

4th. Economy of collection

5th. Elasticity

6th. Probable productiveness

7th. Incidence, or fixedness as to who actually pays the tax.

It is the application of these principles to which all sane and enduring legislation must be directed.

While the subject assigned me is the taxation of Credits and Moneys, I have deemed it advisable to briefly review the history of taxation in Minnesota, founded as it is on the general property tax which includes the assessment of both credits and money.

In this discussion of the subject of taxation of "credits and monies," I have taken the definition of the Minnesota Code of 1905 as a basis. "Credits shall mean and

include every claim and demand for money or other valuable things, and every annuity or sum of money receivable at stated periods, due or to become due, and all claims and demands secured by deed or mortgage, due or to become due."

On the 2nd of March, 1846, there was enacted by the legislature of the State of Ohio a tax law that came to be known as the Alfred Kelly law. This law was incorporated into the constitution of Ohio in 1851 and in 1857, when the constitution of Minnesota was adopted, we took word for word the language of the Ohio constitution as far as it related to taxation. The Alfred Kelly law enunciated no new principles of taxation, but was an enlargement of a system that had been in operation in this country ever since the colonial days.

This tax upon all classes of property of every kind is known to political economists as "The General Property Tax." The theory of this tax, as its name indicates, is that each citizen should contribute to the support of the government in proportion to all the property he owns, real and personal. At first glance nothing seems simpler and more just than this, that the rich man pay more and the poor man less, and each in proportion to his wealth.

The general property tax may be well adapted to an agricultural community, whose property consists almost entirely of tangible property—the real estate of the farm, and with the exception of a small amount of household goods, personal property consisting of the product of the farm, or the horses and implements necessary to work it, but its application to the complex life of a community engaged in trade, commerce and the various other forms of industry which occupy the life of such a community is condemned alike by political economists and practical men of affairs.

In no other country of a high civilization, but the United States, are credits regarded as an actuality, nor

is there any attempt made to levy a direct tax against them. Mr. David Wells in his work entitled "Theory and Practice of Taxation," says—"The general property tax has been in such general use in this country that it is only by a continuous campaign of education that we may hope to eliminate from the minds of our people, and especially that portion of it that enact laws, the idea that now prevails in the United States, but in no other country. 'That Nothing can be "Something" if provided so by statute.' "

For the purposes of this paper I have arranged the subdivisions as follows:

Mortgages
Bonds
Stocks
Public Bonds
Secured and
Unsecured Debts
Monies.

What is a Mortgage?

"A mortgage of lands is a conveyance thereof by way of pledge for the security of debt and to become void upon payment of it." When it comes to taxation of real estate the State declines to consider whether the real estate is mortgaged or not, for the purpose of taxation the State regards all real estate as unincumbered; it ignores the fact that real estate owners do mortgage their property.

This is unjust to those who are compelled to go into debt because the State should always regard the truth. But when the owner of real estate in Minnesota does mortgage his property the State proceeds to punish him by charging a registry fee of one-half of one per cent for recording it. which fee is, of course, always paid by the mortgagor and never by the mortgagee. I pre-

sume the theory of this is "And from him that hath not shall be taken away even that which he hath."

Minnesota is nevertheless far in advance of most of the States as respects the taxing of mortgages, as they go out and find the mortgagee, and if he happen to be a resident of that State they attempt to tax him on an average of about 50 per cent of the income received from his loan, thereby punishing him for lending the money, precisely as though he was a violator of the law.

Take for illustration a piece of property worth $100,000.00, the owner borrows $50,000.00, giving his promissory notes therefor secured by mortgage on the property. The owner of the property, the mortgagor, still continues to pay taxes on the full value of his property, viz., $100,000.00, and the mortgagee pays taxes on $50,000 of promissory notes. Thus does the magic of the general property tax law create for taxation property that does not exist. What is the result? The mortgage is usually taken in the name of a non-resident from whom the mortgagee holds a power of attorney, he taking an assignment back which he does not record. or instead, the loaner sends his money into another State and gives his home field to the loan agent, who, representing as he does foreign capitalists and taking loans in their names, thus escapes all taxes, and in the meantime the borrower is put to an additional expense as the rate of interest is placed high enough to cover taxes, and a little more, on the theory that taxes will be paid on the mortgage, when in fact they never are.

The State of California has an entirely distinct and peculiar method of taxation of mortgages. Provision is made by the laws to compel the mortgagee to pay a tax upon the amount of the mortgage, and to require of the mortgagor a tax upon the value of the mortgaged property less the amount of the mortgage. An agreement by the mortgagor to pay the tax is declared to be

void and the mortgagee is made liable to suffer loss of the interest as a penalty for entering into such an agreement; note the result, mortgage interest rates are higher in California than in any other State of the Union, conditions considered, while in Delaware, which has entirely exempted mortgages from taxation, mortgage interest rates have reached the lowest figure of any State in the Union. Or again, taking two counties on the western line Massachusetts and the adjoining two counties on the eastern line of New York, the conditions being the same, all four being farming communities.

In New York, prior to 1905, mortgages were taxed the same as other personal property, and the average rate of interest in the two counties was 5.88 to 6.12 per cent, while in the two Massachusetts counties, where mortgages are not taxed as such, the average rate was 5.56 per cent, showing conclusively that the interest charges were loaded about one-half of one per cent to cover the tax risk.

If it were not true that the tax rate is added to the interest charge, the rate of interest would have been lower in New York than in Massachusetts, as money is cheaper in New York than in Massachusetts.

The interest rate in New York, under the different systems of taxation, also proves that the borrower pays the tax.

Under the general property tax, when few mortgages were given in for taxation, the average mortgage interest rate in New York City was 5.12 per cent.

On July 1, 1905, a law went into effect in New York taxing mortgages 50 cents per annum for each one hundred dollars or major fraction thereof, a much less rate of taxation than on other property, and yet the mortgage interest rate increased in the next year to 5.54 per cent, a net increase of .42 per cent, an amount nearly equal to the entire tax.

On July 1, 1906, the system was changed to a recording tax, of 50 cents per hundred or major fraction thereof to be paid only once. Under this plan the mortgage interest rate decreased to 5.15 per cent, and this, too, in spite of the fact of an unusual stringency in the money market.

I have referred to the registry tax on mortgages. I believe Minnesota made a great advance in taxation when the last legislature passed that law; next to total exemption from taxation is the law providing for a low rate. Men will pay what is fair taxation, but will not submit to what amounts virtually to an arbitrary seizure of private property.

I saw recently what to me was a splendid object lesson as to the working of the registry tax law. In September a friend of mine, a country banker in this State, told me of a loan they had against a large city concern, it had run a year at 5½ per cent, and they had just renewed it for a year at 7½ per cent. The same week I went to the Minnesota Loan and Trust Co. of this city to try and get some 6 per cent farm mortgages for a client, but the best I could do was 5½ per cent. They said to me. "You know these are tax free; however, we have some in North Dakota. about ten miles from the Minnesota line, that will pay 6½ per cent." There were two object lessons. First. farm mortgages 2 per cent lower than the best commercial paper, both Minnesota concerns and a Minnesota mortgage paying 1 per cent less than a North Dakota mortgage because the Minnesota loan was practically tax free. Here is a condition existing that cannot help but be of advantage to Minnesota, if our farmers can borrow money cheaper than those in neighboring States, it means greater prosperity for them, and prosperity for our farmers means good times for the rest of us. I trust that by the time the next legislature meets the object lesson of the last

two years will result in the abolition of all taxation of mortgages.

In Hennepin County the amount of taxes collected under the old law for 1906 was $5,000.00, while under the registry law there was collected from May 1st to Dec. 1st the sum of $42,320.66.

Bonds

Bonds are of two classes—private bonds such as are issued by railroads and mercantile companies, and public bonds, such as are issued by a State, or some political subdivision thereof. If a railroad or a mercantile company in this State issues a bond, the money paid for it is used by the company for the improvement of its property, and upon this property the State collects its taxes. The bond is but a piece of paper, an evidence merely of indebtedness for the money. To tax the property into which the money has gone, and also the bond which is an evidence of the indebtedness is double taxation.

If the bond is issued by a private corporation outside the State, the money from the bond goes into the property of the corporation in the State from which it is issued, and the property of the corporation being taxed in that State, to tax the holder of the bond in this State is to double tax the same property.

Stocks

Certificates of stock issued by corporations outside the State of Minnesota occupy the same position as that of bonds issued by such corporations. The corporations pay taxes on their property where located.

A certificate of stock held by an owner in Minnesota is merely evidence that he is a part owner of this property which is located in another State.

To tax the property in the other State whose ownership the certificate evidences and then tax the owner in Minnesota on the certificate is double taxation.

If a man owns a farm in North Dakota and has a deed in this State that deed, which, like the share of stock, is a mere evidence of ownership, is not taxed. The injustice of so doing would be apparent to any one, yet the same person who admits the injustice in that case will assert the righteousness of taxing the certificate of stock.

Let us take a concrete case covering the question of stocks and bonds. Mr. A, a resident of Minneapolis, owned a line of elevators in Nebraska, the business grew, he took in a partner, the business prospered, and, desiring to keep some of their old employes who had threatend to leave, they gave several of them each a small interest in the business. Finally it was decided to incorporate the business. which was done. at once the State of Minnesota steps in, claiming that the certificates of stock were wealth, and should pay taxes in this State. Another elevator company, wishing to retire from business, all of whose houses, 112 in number, were located in Nebraska and Kansas, Mr. A, and his fellow stockholders bought the entire line, it was decided to issue ten year bonds on all the houses to raise the funds wherewith to make the purchase. The bonds were sold, money invested in the other line of elevators, and at once the State of Minnesota steps in and says pay taxes on the bonds that were sold in this State, no matter that the property invested in is all real estate, and all located in other States, so long as you hold a piece of paper, designated as a bond, you must pay taxes on it. If this is not double taxation, what is it?

Incomprehensible as it may seem, it must nevertheless be true that those persons that favor the taxing of stocks and bonds, must believe that somewhere between the time that the partnership ceased and the time that the corporation began business as such, an amount of wealth, was legislatively created equal to the original amount.

This conclusion cannot be established by any possible system of reasoning. The fact is, the only thing that has been created is the sheets of engraved paper showing just what share of the total property is owned by each stockholder and each bondholder.

The same rule holds good even if the stock and bonds had been issued when the elevators were first built. Instead of one man furnishing all the money, a number of men put in different amounts, and the stocks and bonds issued to show the share owned by each.

Take any corporation and there would be no loss of property if all the stocks and bonds were retired and the corporation changed into a partnership, or individual ownership.

Public Bonds

Bonds issued by the State or any political subdivision thereof should never be taxed. Any tax to which bonds are subjected, is added to the interest rate and comes directly from the tax payers. At the present time the city of Minneapolis is advertising for sale some 4 per cent bonds, and this is the third time since last May that these bonds have been offered to the public. If any resident of Minnesota were foolish enough to buy any of these 4 per cent bonds, on the 1st of next May he would have the State of Minnesota at his door in the person of a deputy assessor asking for about 3 per cent tax on those same bonds. Now note the difference, last year the legislature of Ohio exempted all such bonds from taxation and last fall, when the city of Cincinnati offered for sale $300,000.00 of 3 per cent bonds they were over subscribed three times, and all by her own people. Is it not better for Cincinnati to pay out that interest to her own people than to do as Minnesota cities are compelled to do by reason of her tax laws and send her interest East each year.

SECURED AND UNSECURED EVIDENCE OF DEBT

"A promissory note is but the signed promise of one party to another to pay a certain sum of money at a specified time." The owner of this signed promise has either transferred to the debtor goods or money or performed labor for him. The goods are certainly taxed wherever they are found; the money loaned has gone at once into tangible, real or personal property which is taxed, and the labor performed has been expended in improving tangible, real or personal property whose value has thereby been increased, and taxes collected on its value as so increased.

It is, therefore, plainly evident that all the objections that apply to the taxation of credits apply quite as well to the taxation of promissory notes.

If A. sells a donkey to B. and takes his promissory note and B. sells the donkey to C. and takes his promissory note, there is only one donkey in the deal, yet the assessor says there are three and levies taxes on three donkeys. Is there not a fourth donkey untaxed?

Efforts have been made, and some results secured, in a number of States to reform the law relating to taxation of secured credits, but for some unexplainable reason no results seem to have been secured in any State, except Delaware, to exempt unsecured credits from taxation.

The late commission of California came to the conclusion that these unsecured debt obligations were in no sense property and were not suitable for taxation, and gave their reasons for so finding in language that could not be misunderstood, still for fear the main issue, which was the separation of State and local taxation, might be lost sight of in the discussions that were sure to arise, advised that nothing be done at the time and that the old rule be retained.

Such a conclusion is hard to understand except on the grounds of expediency. If mortgages, stocks and bonds

which are at least to some degree subjects of public record, ought not and cannot be located for taxation, what possible excuse is there for attempting to tax these other evidences of indebtedness which can be carried around in the pocket or locked up in a vault and no one but the maker and the owner be any the wiser on account of the transaction.

Let us take for illustration a Minneapolis jobber; he sells on the tenth of April $2,000.00 worth of goods to a dealer at Fergus Falls, taking his 90-day note in payment for the same. The goods are in possession of the country merchant on May 1st, and he is taxed accordingly. The note is in possession of the city jobber, and he is taxed on the note. Thus the State levies taxes on $4,000.00 worth of property when only $2,000.000 of property is in existence, or ever had been, or ever will be. Thus by the wonderful working of the general property tax do we again get something for nothing. If the jobber had sold to a merchant at Fargo, the goods would be taxed in North Dakota. By what right, except that of might, can the State of Minnesota tax the jobber the same as though he still had the merchandise in his store. The goods are in fact no longer there, he has his debt in its place, something that is neither a tangible, nor visible thing; to tax this debt as if it were merchandise when the merchandise, which was sold, whereby the debt was created, has been transferred to another State, and taxes paid thereon, is simply double taxation.

Even if these goods had been sold on open account, without note, the principle involved would be exactly the same.

Moneys

In 1884 the moneys listed for taxation in this State amounted to $2,236,652.00 and the bank deposits amounted to $27,339,949.00 so we levied taxes that year on

nearly ten per cent of the money on deposit; twenty-three years later, 1907, we had returned for tax purposes in round numbers $8,000,000, and the reports of the Comptroller of the currency and the state examiner show that on May 20th, 1907, there was on deposit in the banks and trust companies of Minnesota $192,804,211.93, so that the amount returned in 1907 was a fraction over four per cent of the deposits. If, after twenty-three years we have been able to tax but four per cent of the money in the State, how long is it going to take us to tax the other 96 per cent. And yet, probably the most suicidal policy that could be carried out in Minnesota would be to attempt, just once, to tax bank deposits, for after that one trial, every bank in the State would be in a bankrupt and insolvent condition. And how could this be otherwise. Banks pay 3.5 to 4 per cent interest; the tax rate in Minneapolis for the coming year is to be 3 per cent, in a city of five thousand inhabitants, a little over one hundred miles west of here the rate is 5.5 per cent, while in another. seventy-five miles south of the Twin Cities it is 7.4. Does any sane man believe for one instant there would be any money left in the banks in these cities on May 1st. We have had an illustration recently of the rapidity with which money can go into hiding, but the example we have had would compare with the speed with which it would disappear if an attempt were made to tax it, about as a farm horse could travel against a 90-horse power automobile.

It should be remembered that money is not wealth. but only the evidence of wealth; it is manifestly improper to tax both the wealth and the representative thereof.

As a result of the attempt to enforce the general property tax, let us consider for a moment what classes of property we have reached so far as it relates to the taxation of moneys and credits.

1. We have taxed all the property of the widows and orphans when they get into the probate court.

2. We continue to tax all the property of orphans so long as they remain under guardianship.

3rd. We got a small percentage of the property of the wealthy man, who gives in just as little as he dares and keeps the assessor from asking embarrassing questions.

4th. The first credit of the working man, who ignorant of the "taking way" of the tax laws, makes a return of it to the assessor. This never happens but once, for having learned his lesson, he takes good care that the property is put in such shape that the taxing authorities cannot find it a second time.

And lastly, we get a very, very small amount from men, whose consciences will not permit them to evade the raids of the assessor. That is the sum and substance of it when it comes to the taxation of credits and money. We have taken a large proportion of the taxes received from this class of property, from those who can least afford to pay it.

Furthermore, we have added a burden to every man in the State who has had to borrow money, and in so doing we have curtailed in a greater degree the development of our State, for everything that makes money dearer tends to stay the progress of the people of a community, no matter whether it is the manufacturer or merchant who borrows to increase his business, the working man who borrows to build a home, or the farmer who borrows to improve his land.

Let us consider further, if you please, some of the results accomplished in a State that has probably made the greatest effort of any State in the union to tax credits and money. I refer to the State of Ohio. The Ohio law provides that the taxpayer shall make a sworn statement of all property owned; it further provides that in case this statement is not forthcoming, the assessor shall

make an arbitrary assessment, which, when made, shall be doubled. To supplement the work of the regular taxing authorities they had in force over twenty years, until three years ago, when the law was declared unconstitutional, what was known as the inquisitor or tax ferret system, that is, the county commissioners were authorized to make contracts with outside parties, to ferret out property that had not been properly listed, for which they were to receive 20 per cent of all moneys collected as taxes by reason of their findings. The result was, blackmail ran riot in all parts of Ohio, for men would take the chance of evading their taxes, knowing that if found out they could settle much more cheaply with the ferret than it would cost them to pay their taxes. And here are a few of the results accomplished under the drastic Ohio laws.

In 1851 in Hamilton County (that being the county in which Cincinnati is situated) the amount of credits and money returned was $3,292,989.00; in 1903, fifty years later, the amount of credits and moneys returned was $3,153,350.00, being $139,636.00 less than was returned in 1851. Again, the amount of money returned in Hamilton County in 1866 was $6,778,883.00, while in 1896, thirty years later, it was $1.097,283.00.

Again, the amount of money on deposit in Cleveland banks in 1896 was $70.000,000.00, and of this there was returned for taxation $1,741,129.00. In California, in 1906, the moneys and credits comprised only 2 per cent of the entire assessment and included in this was the surplus credits over deposits of the banks.

In Wisconsin in 1904 the credits and moneys comprised only 5.33 per cent of the entire assessment, and this included all mortgages. The per cent of moneys and credits given in for assessment is equally small in all the States.

The California tax commission uses these words in

speaking of the assessment of credits and money. "Our present system is a school for perjury, it puts a penalty on honesty and pays a high premium for dishonesty. The burden of the support of the government falls most unequally upon those who should bear it. It falls with special severity upon the poor and with greatest severity upon the honest."

Any governmental policy that corrupts our political consciences, that makes liars out of our people, that puts a premium on perjury, that places a penalty on honesty, that is universally evaded, that is evaded by and with the assistance of public officials, and that cannot be enforced even with the most drastic penalties, is a bad policy and should be changed. In every State the law taxing moneys and credits is held in utter contempt. No one is expected to comply with its provisions and these expectations are fully lived up to.

The general property tax, too, is today condemned by nearly every American writer on political economy, as well as by the practical men of affairs who have studied it or been called upon to enforce it.

Mr. David A. Wells says:

"The general property tax should be modified and even eliminated as far as possible. The general principle underlying it of taxing every form of property was suited only to a time when the bulk of a man's estate consisted in visible and tangible objects—lands, houses, live stock and furniture. With every creation of a credit investment, with the immense development of corporations, the principle has become weaker, until it now stands confessedly inapplicable to at least four-fifths of the personal property in existence, and this proportion grows larger each year."

Professor Seligman of Columbia University, in his work "Essays on Taxation," says:

"Practically, the general property tax, as actually ad-

ministered today, is, beyond all peradventure, the worst tax known in the civilized world. It puts a premium on dishonesty and debauches the public conscience; it presses hardest on those least able to pay; it imposes double taxation on one and grants immunity to the next. In short, the general property tax is so flagrantly inequitable that its retention can be explained only through ignorance or inertia. It is the cause of such crying injustice that its abolition must become the battle cry of every statesman and reformer."

Prof. Richard T. Ely, in his report to the General Assembly of Maryland in 1888, said:

"I have first to remark that the one uniform tax on all property as an exclusive source of revenue, and the chief source, though main feature, in direct taxation, never has worked well in any modern community or State in the civilized world, though it has been tried thousands of times, and although all the mental resources of able men have been employed to make it work well. I have read diligently the literature of finance to find an example, but in vain, and, lest this should not be sufficiently trustworthy, I have made it my business, in my capacity as tax commissioner, to visit typical States and cities and to make inquiries in person of citizens, as well as of officials entrusted with the administration of the laws. I have visited Charleston, S. C., Savannah, Atlanta and Augusta, Ga., Columbus, O., Madison, Wis., Toronto, Montreal and Quebec, Canada, and the result has been abundantly to confirm all that I have said about the impracticability of the one uniform tax on real and personal property."

But you may say these men are political economists, writers of books, theorists. Let us summon as witnesses, then, the practical men.

The taxing officials in New York State are unanimous in their condemnation of the general property tax.

Citations innumerable could be made from their reports. The following from the assessors' report of 1870 is characteristic of them all:

"The general property tax is a reproach to the State, an outrage upon the people, a disgrace to the civilization of the nineteenth century, and worthy only of an age of mental and moral darkness and degradation, when the only equal rights were those of the equal robber."

THE MORTGAGE REGISTRATION TAX LAW

By Ambrose Tighe.

Philosophically, there would not seem to be much justification for the taxation of any credits. A. lends B. a thousand dollars. B. either keeps the money or invests it in other property. The only entity which exists at the end of the transaction is the thousand dollars which A. originally had, and which B. now has in the shape of money or the property in which he has invested the money. When the money or property in B.'s possession is taxed, all that exists is taxed. B.'s promise to return the money to A. has no physical being and is not property.

If credits should be taxed, philosophically there would not seem to be much justification for taxing credits secured by real estate mortgages, differently from credits secured by mortgages on personal property or credits not secured by any specific lien. Almost every man who succeeds in borrowing is in effect mortgaging his property, real or personal. He may not give a specific lien on it. But whoever trusts him, has in mind his assets and extends him credit with the expectation of having recourse to them, should it be necessary. If the debtor pays the tax, as he does in most cases where a tax on credits is actually enforced, a credit without specific security has elements of value, responsive to taxation, which are greater than a credit secured by mortgage, because it takes more qualities of character and reputation to get it.

The so-called science of taxation, however, has little more philosophy in its composition than it has poetry. It is made up chiefly of what is customary and practically convenient, and what is countenanced by the courts because it is customary and practically convenient. The State has to be supported and it grabs where it can and what it can for the purpose within constitutional limitations, leaving the objects immediately preyed on to diffuse the levy by preying on others. In this spirit, while there has been little attempt to collect taxes from credits unsecured or secured by chattel mortgages, people generally have felt that real estate mortgages should be taxed, and the courts have sustained statutes providing machinery for their taxation. The New York mortgage registration tax law has been sustained by the New York courts, although it applies to real estate mortgages only. (People vs. Ronner, 77 N. E. 1061). The Minnesota mortgage registration tax law has been sustained by a Minnesota trial court, although it applies to real estate mortgages only. The New York law is now before the Supreme Court of the United States, and the Minnesota law will probably get before our Supreme Court. If their decisions are controlled by the same considerations, which have heretofore been held pertinent in such controversies, they will also probably be upheld by these higher tribunals.

When the 1907 Minnesota legislature convened, the wide open tax amendment was thought to have been adopted. This emancipated the law making powers of the State, as far as tax legislation was concerned. Before that event the constitution stood in the way of most revenue raising reforms. After it, almost any old measure would be constitutional. For a quarter of a century the inequalities and absurdities of our taxing system had been a subject of debate. Even the son of a prophet would have predicted that when the barriers were re-

moved, there would be a flood of bills designed to bring about better things. The pent up thought of the commonwealth would reasonably have been expected to express itself pretty audibly. But it did not. The first fruits, and for that matter about the only fruits of them that had slept so long was the mortgage registration tax law. There seemed to be a popular demand for it, and it was about the only measure for which there seemed to be an effective popular demand. Some other revenue measures passed the house, but only as the result of much labor. A good many were defeated in the house and all which passed the house. except the mortgage tax law, died in the senate. The State, which had been panting for tax reform, was afraid of it, when it could get it. But it did want a mortgage registration tax law.

On the 16th of January, Mr. Nimocks of Minneapolis, introduced the first bill on the subject H. F. 33. On February 5th, Mr. Sawyer also of Minneapolis, followed this with another bill, H. F. 275. On February 13th, Mr. Brady of St. Paul introduced a third bill H. F. 364. On February 20th, Mr. Thayer of Fillmore County, introduced a fourth bill, H. F. 474. There may also have been others on the same subject. The first three bills were all based on the New York Law (Laws 1905 c. 729, Laws 1906 c. 532) and were very elaborate in their provisions. In general they provided for one tax to be paid at the time of recording. Mr. Thayer's bill provided for an annual income tax to be paid on all unsatisfied mortgages of record.

When the tax committee took these bills under consideration, there was little difference of opinion on the proposition that there must be a real estate mortgage registration tax of some sort. The arguments against it were not overlooked. Their force was admitted. It was admitted. for example, that the borrower would in most

cases pay the tax, and that it would, therefore, in effect only be an additional tax on real estate, which, in many sections of the State, was already burdened enough. But the committee felt constrained to yield to public opinion. The borrowers, who are in a majority always, have from time immemorial been prejudiced against the lenders. They are so prejudiced that sooner than have mortgages untaxed, they prefer to pay a tax on them themselves, and the committee decided to recommend that they be permitted to. But I think the general sentiment of the committee favored going no further than it had to. Mr. Thayer's bill for an annual tax received no endorsement. was reported out without recommendation through courtesy to its author only and was indefinitely postponed by the house on general orders. The services of Mr. Daniel Fish of Minneapolis were enlisted to draft a practicable measure out of the other bills which had been introduced. Without compensation and from patriotism he prepared Chapter 561 of the laws of 1907, and it passed the house unanimously, and the senate with a few dissenting votes. Many members who voted for it, did so because they believed it provided for as small a tax as public opinion would sustain on a species of property which should not be taxed at all.

One of the difficulties in the way of intelligent tax legislation in Minnesota has been the lack of a statistical department. There is a mass of information in the various offices in the capitol, and there are courteous and capable employes to make it as accessible as they can. But there has heretofore been no one whose duty it was to get this in shape for use by legislative committees or to supply omissions. When a tax bill is before parliament or congress it is possible to state with a high degree of accuracy what amount of revenue it will produce. The probable revenue producing power of a tax bill pending before the Minnesota legislature is seldom given

much consideration, for one reason because it is impossible to make even an intelligent guess as to what it is going to be. This is a situation not peculiar to Minnesota, but is common to most of the States. Not only is this true, but even after a tax law has been in operation in a State, it is a hard matter to learn what revenue it has produced. The figures are apt to be hid in reports which cannot easily be found, and there is practically no general literature on this aspect of the taxation problem. As far as Minnesota is concerned, the work of the permanent tax commission will probably go a long way towards supplying what is here needed. But the 1907 legislature had practically nothing to guide it except the experience of Mr. Iverson, the able State auditor. To illustrate, several measures were introduced in reference to the taxation of sleeping car companies. Some of these provided simply for an increase in the rate of gross earnings tax, and others provided for taxation on a mileage basis. There was no information at hand as to which would give the largest return. The interested legislator was left to figure it out as best he could, and he could not figure it out at all. Finally Chap. 453, Laws 1907, was enacted, which included both systems, and extended sleeping car companies the option of accepting which either it pleased. There is not much doubt that it will accept the one which yields the smaller revenue. The legislature, in the same way, had no mother to guide her in estimating the revenue results of the mortgage registration tax. Several members got statistics from the auditors of their counties. I got the St. Paul Real Estate Exchange to make some investigations. It was stated, but on what authority I don't know, that $28,000,000 of mortgages had been recorded in Hennepin County alone in 1906, which at the rate of one-half of one per cent would mean a return of $140,000. The St. Paul Real Estate Exchange's fig-

ures were much smaller, and suggested a revenue in Ramsey county of about $25,000 a year. None of the figures gave any hint as to the probable result from the taxing of executory contracts of sale, and in the nature of things nothing could be learned about this, because such contracts are not usually recorded.

I have taken the trouble to inquire of all the county treasurers of the State as to the revenue results of the act for the first six months of its operation, that is, from May 1st, 1907, to November 1st, 1907. I have received the figures from all the counties except Clay, Clearwater, Mahnomen, Olmstead, Sherburne and Todd. Omitting these, the gross returns for the six months were a little short of $149,000. Assuming that they shall be as great during the next six months, there is thus disclosed an annual revenue of $300,000. Hennepin county, of course, shows the biggest figures, $37,521.66, or about half of what was predicted. Ramsey county is next with a little less than $15,000, which is somewhat larger than was predicted. St. Louis county is nearly as large in return with nearly $13,500. Winona county comes fourth with $4,700, and Lake county fifth, with $3,972,- both of these figures being probably explained by the recording of some unusually large trust deeds. The richer and older agricultural counties, with here and there an exception, run surprisingly even, the figures in most cases being somewhere around the $1,000 mark. The smallest returns are from Cook county, where only $84.00 were collected. Several of the county treasurers in sending me their statistics have commented on the law. Some of them who have done so have expressed the opinion that the revenues from mortgage taxation are less under the new law than they were under the direct system, which can hardly be counted a serious criticism, and all of them say that in practically every case, the bor-

rower pays the tax which accords with what was expected.

The law itself is, in my judgment, well drawn. It has the simplicity, directness and condensation of its author's work in this line. If any criticisms are to be made, they probably may be confined to the following points:—

(1) The law is not very effective as far as executory contracts of sale are concerned. I do not believe much revenue has been derived from this source. The act does not make them void unless the tax is paid, but simply provides that unless the tax is paid, they shall not be recorded, be received in evidence, or have validity as notice or otherwise. This permits the parties to postpone the payment of the tax, until one or the other of them wants to record the contract, or litigation is impending, which means that in most cases, the tax need never be paid.

(2) There is no provision in the act as to the payment of the tax on mortgages given to secure future advances, which is a form of mortgage more common than is generally understood, or as to the payment of the tax on mortgages given by way of indemnity against contingent liabilities on the part of sureties, particularly bonding companies.

(3) I think some difficulties are likely to arise out of the third section of the act. This exempts mortgages taken in good faith by persons or corporations whose personal property is exempt from taxation, or who pay a gross earnings or other form of commuted tax in lieu of all other taxes, but it further provides that the payment of the tax on the mortgage shall not exempt it from the operation of the laws governing the taxation of banks, savings banks or trust companies. The first provision referred to was urged in the first litigated case under the law by a life insurance company as a basis of exemption, it claiming that the two per cent on premiums

tax was in lieu of all other taxes. The second provision referred to has no very clear meaning. There are no special laws governing the taxation of banks, savings banks and trust companies. They are taxed theoretically like other corporations. I do not know what Judge Fish intended by this language. As the law reads, a mortgage loan company, or an individual, cannot be taxed by the ad valorem method on mortgages which have paid the registration tax. Is his idea that in listing their assets, banks, savings banks and trust companies shall be required to list and pay taxes on mortgages which have paid the registration tax? If this is the purpose, the provision is probably unconstitutional. If it is unconstitutional, it suggests one effect of the law which was not fully realized when it was enacted. Mortgages are a favorite form of investment by banks, especially in the country, savings banks and trust companies. If all the taxes heretofore paid on them by such institutions as parts of their assets are eliminated from the tax rolls, there is going to be a very considerable offset to the $300,000 a year which the law appears to have added to the States' income.

In conclusion, I think the law in spite of all which may be said against it, will have one good effect anyhow. It will call attention to the fact that the State and its subdivisions can be supported otherwise than by the direct taxation of real and personal property, and educate the people to the possibilities of a happier system when almost the full burden of public taxation will not fall, as it does now, on the farm, the homestead and the personal property of the widow and the orphan.

THE BANKER'S VIEW OF THE MORTGAGE REGISTRY TAX

By A. D. Stephens.

I cannot understand why a banker's view should be desired on the Mortgage Registration Tax, unless it be that at the time of the passage of the bill there was some opposition to it from bankers who feared that it would take money out of the banks by depositors who would loan it direct without using the bank's agency, but that I considered as an unfair opposition, because if the law would have the tendency of placing the lender and borrower where a middle man would be unnecessary, the law would then be an advantage to the people at large.

The fear of the bankers, however, has not been realized in this community, nor do I think it has in any part of the State, but if it had been, the banker would be entitled to no consideration, nor would he need any, because the banker's compensation, if it is of value, comes from the fact that he is a better judge of credits, and with or without the law the money lender will use the bank, either by placing his money on deposit, and allowing the bankers to reloan it at a higher rate, or the lender uses the bank as his agent to place the money direct, and the banker's compensation in either case is well earned in the additional safety to the lender, and in cases where the money is loaned directly for the lender in collecting and remitting the interest. The law should be considered as it effects all the people, and not any class. The accepted theory of all taxation is that it must or should be equal. That fact is evidenced by the constitution of this and other States, as well as by the national consti-

tution, the provisions of the constitution being carried out in enactments, with the exceptions of special taxes in the way of license fees and poll tax.

Underlying this theory, however, there is another not so clearly set forth, and probably caused by the knowledge that absolute equality cannot be obtained. This sub-conscious theory is that if there must be inequality, that such shall be to the benefit of the poorer citizen, who is least able to pay taxes. This is evidence by the law in this State, and in most other States allowing an exception of some certain amount to be deducted from the assessment by the authorities, and always such sum is to be deducted from every assessment, and not from a higher assessment only, and thus giving a greater per cent of exemption to the poorer tax payer.

The mortgage registration tax complies with neither of these theories. It is unequal from almost any point of view taken. It costs the same whether the mortgage that pays the tax bears a high or low rate of interest; whether the mortgage runs for a longer or shorter time; whether the security is safe or only reasonably safe, or practically worthless, and the tax alltogether opposes the theory that any inequality in the tax inures to the benefit of the poorer men, as in practice the tax is nearly always paid by the needy borrower, and in very few instances by the more wealthy lender.

Perhaps the law can be better understood by knowing something about why it was passed, and my opinion is that it received many votes in the legislature by those who do not believe in taxing credits at all, and even if they did, do not believe in a tax especially on mortgages, which seems to be simply an attempt to discover "ability" to pay, as there can be no justice in taxing a debt secured by mortgage, and allow another debt of equal safety, and as high a rate of interest, simply evidenced by a promissory note to escape taxation. The consti-

tution, however, made it impossible to pass such a law in this State, so the members of the legislature of this mind voted for the bill, because it would to a large extent exempt mortgages from taxation. It is true that former laws did and do provide for the taxing of all credits, but the law was a dead letter, and will probably continue a dead letter for lack of enforcement, so that all that can be said for the Registry Tax is that it makes the status of the taxing of mortgages definite and certain, and leaves the lender in a position where he cannot be harrassed by the tax ferrett or the occasional zealous assessor, which would compel the lender to pay a heavy tax in one county, and altogether escape in another.

An argument for the bill was that it would raise a certain large amount of revenue. That argument has turned out to be true. In fact from what statistics I have seen I believe it is raising a larger revenue than was anticipated by the legislature, but that fact is no reason for approval of the law, as it will be conceded that the State government has not right to place extraordinary taxes except in extraordinary needs, and while it is true that many forms of taxation have begun as emergency measures, (such as revenue taxes, and even the personal property tax itself,) there was at this time no need to create an unequal tax for the purpose of revenue. Another objection to the tax is that it is really a tax on business. Such taxes are justified only as police regulations, like for instance the liquor license, and others of that nature, and it does seem to me that this tax, placing a burden on one class of business transactions, is utterly unjust and unfair. Why should the borrower (because he is the one who pays the tax) who is compelled to give a mortgage, pay a tax, while the borrower whose credit is good enough so that he can borrow without giving a mortgage, not pay any, so that it is really a restriction on a legitimate business. The mak-

ing of a mortgage does not create any additional property, nor any increase in wealth, and it would seem proper that since the constitution demands some taxation of credits, and it is a well-known fact that all other forms of credits pay very little, if any, taxes, that the registration tax should be reduced to a minimum of, say, five cents on every one hundred dollars, which would not make it just, but would make the burden of taxation on that class of business so small that it would not be a burden to the borrower. Having always looked upon an income tax as the most just tax, it would seem from my point of view, that a law be enacted to compel the payment of a certain tax on the amount of interest actually collected by the lender. Such a tax could at least be made much more equal.

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